

REPORT BY THE
AUDITOR GENERAL
OF CALIFORNIA

**A REVIEW OF
THE FINANCIAL CONDITION OF SCHOOL DISTRICTS,
COUNTY OFFICES OF EDUCATION, AND COMMUNITY
COLLEGE DISTRICTS IN CALIFORNIA**

REPORT BY THE
OFFICE OF THE AUDITOR GENERAL

F-637

A REVIEW OF THE FINANCIAL CONDITION OF
SCHOOL DISTRICTS, COUNTY OFFICES OF EDUCATION,
AND COMMUNITY COLLEGE DISTRICTS IN CALIFORNIA

MARCH 1987



Telephone:
(916) 445-0255

STATE OF CALIFORNIA
Office of the Auditor General

Thomas W. Hayes
Auditor General

660 J STREET, SUITE 300
SACRAMENTO, CA 95814

March 24, 1987

F-637

Honorable Art Agnos, Chairman
Members, Joint Legislative
Audit Committee
State Capitol, Room 3151
Sacramento, California 95814

Dear Mr. Chairman and Members:

The Office of the Auditor General presents its report concerning the financial condition of school districts, county offices of education, and community college districts (local education agencies). Many local education agencies are facing financial problems because of poor fiscal management. In addition, the reporting system used to identify school districts and county offices of education that are having financial problems needs improvement.

Respectfully submitted,

Thomas W. Hayes
for THOMAS W. HAYES
Auditor General

TABLE OF CONTENTS

	<u>Page</u>
SUMMARY	S-1
INTRODUCTION	1
AUDIT RESULTS	
I MANY SCHOOL DISTRICTS, COUNTY OFFICES OF EDUCATION, AND COMMUNITY COLLEGE DISTRICTS ARE FACING FINANCIAL PROBLEMS	9
CONCLUSION	35
RECOMMENDATIONS	36
II THE EARLY WARNING SYSTEM TO IDENTIFY SCHOOL DISTRICTS AND COUNTY OFFICES OF EDUCATION WITH FINANCIAL PROBLEMS NEEDS IMPROVEMENT	37
CONCLUSION	47
RECOMMENDATIONS	48
APPENDICES	
A DISTRIBUTION OF RATIOS OF FUND BALANCE TO EXPENDITURES FOR 124 LOCAL EDUCATIONAL AGENCIES AS OF JUNE 30, 1986	51
B JUNE 30, 1986, FUND BALANCE AND FISCAL YEAR 1985-86 REVENUES AND EXPENDITURES FOR 124 LOCAL EDUCATIONAL AGENCIES	57
C AVERAGE DAILY ATTENDANCE 124 LOCAL EDUCATIONAL AGENCIES FISCAL YEARS 1981-82 THROUGH 1985-86	59
D ASSUMPTIONS WE USED IN PREPARING FUND BALANCE PROJECTIONS FOR THE EIGHT LOCAL EDUCATIONAL AGENCIES WE VISITED	63

TABLE OF CONTENTS (Continued)

	<u>Page</u>
RESPONSE TO THE AUDITOR GENERAL'S REPORT	
State Department of Education	65
Board of Governors of the California Community Colleges	69

SUMMARY

RESULTS IN BRIEF

Many California educational agencies will be unable to overcome unexpected losses of revenue or unexpected increases in expenses because they have depleted their reserves by spending more than they receive in revenue. Thirty-one of the 132 local educational agencies (LEAs) we reviewed had low reserves at June 30, 1986, and 15 of these repeatedly spent more than they received in revenue. As a result of this trend, since fiscal year 1981-82 the State has approved emergency loans totaling \$23.9 million to 12 LEAs. These problems have occurred because some LEAs base their budgets on inaccurate estimates of their revenue and expenditures and because some LEAs use their general fund to pay for overspending in other funds. In addition, some LEAs have granted salary increases that are larger than the increases in revenue used to pay the salaries. Finally, excessive administrative costs and declining attendance have contributed to the declining reserves in some of the LEAs.

More LEAs may require financial assistance from the State if they do not promptly identify and correct their financial problems. Recent legislation established an early warning system requiring school districts and county offices of education (county offices) to assess their financial condition and recommend actions to correct the problems they identify. However, many county offices are not submitting the required certifications, or the school districts and county offices submit certifications that do not accurately reflect their financial condition. Further, many of the reports are late and incomplete.

BACKGROUND

The State operates a large public school system that serves approximately 4.6 million students in kindergarten through grade twelve (K-12) and over one million students in community college districts throughout the State. The K-12 education system is administered by the State Department of Education (department), 58 county offices, and 1,028 school districts. The community colleges are operated by the Board of Governors of the California Community Colleges and 70 locally governed districts.

Since the passage of Proposition 13 in 1978, the State has provided approximately 65 percent to 68 percent of the LEAs' revenue. In fiscal year 1986-87, the State will spend approximately \$14 billion on LEAs, 43.5 percent of the State's General Fund budget.

PRINCIPAL FINDINGS

Many School Districts, County Offices Of Education, and Community College Districts Are Facing Financial Problems

We analyzed the fiscal year 1985-86 financial statements of 124 LEAs to determine the financial condition of the State's LEAs. In fiscal year 1985-86, 25 of the 124 LEAs had low financial reserves, and 25 spent more than they received in revenue. In addition, we analyzed the spending patterns of 25 of these 124 LEAs during the last three years: 14 of these 25 LEAs spent more than they received in revenue in at least two of the last three years.

To determine the causes of the financial problems that are facing LEAs, we visited 5 LEAs that the department had identified as likely to require financial assistance and 3 LEAs that we had audited before because of their financial problems. Six of the 8 LEAs we visited have low financial reserves, and 4 have spent more than they have received in revenue in at least three of the last four fiscal years. The LEAs' reserves have declined for a

variety of reasons. Seven of the 8 LEAs have had problems budgeting revenues, and 7 of the 8 LEAs have used general fund monies to pay for overspending in other funds. In addition, all 8 of the LEAs have granted salary increases that are larger than the increases in the revenue used to pay the salaries. Unless these LEAs can reduce their expenditures or increase their revenues, we project that 6 of the 8 LEAs that we visited will end fiscal year 1986-87 with a deficit in their general fund.

The Early Warning System To Identify School
Districts and County Offices of Education
With Financial Problems Needs Improvement

Recent legislation created early warning systems to identify LEAs that may be unable to meet their financial obligations. These early warning systems are too new for us to assess their effectiveness. However, there are weaknesses in the early warning system for school districts and county offices that may impede its effectiveness. The system does not provide criteria or standard report forms for school districts and county offices to use to assess their financial condition. In addition, current state law does not give the state agencies that review the reports the authority to ensure that school districts and county offices comply with the reporting requirements of the early warning system or adopt and implement effective corrective action plans. As a result, there is a lack of consistency in the way school districts and county offices assess and report their financial condition. In addition, some county offices do not submit required reports, and many school districts and county offices that do submit reports submit reports that are late or incomplete. If school districts and county offices do not prepare timely, accurate assessments of their financial conditions and identify and correct their financial problems, they may require financial assistance from the State.

RECOMMENDATIONS

To ensure that they are able to meet their financial obligations, local educational agencies should exercise sound fiscal management and maintain prudent financial reserves.

To improve the early warning system and ensure that school districts and county offices of education comply with the reporting requirements of the early warning system and adopt and implement effective corrective action plans, the governor and the Legislature should take the following actions:

- Adopt legislation that requires the State Department of Education, in conjunction with the State Controller's Office and county superintendents of education, to develop criteria that school districts and county offices of education will use to assess their financial conditions; and
- Adopt legislation that provides the State Department of Education and the State Controller's Office with the authority to enforce the requirements of the early warning system.

To ensure that the early warning system for community college districts is effective, the Board of Governors of the California Community Colleges should closely monitor the early warning system to ensure that it achieves the desired results.

AGENCY COMMENTS

The State Department of Education generally concurs with our findings about the high number of school districts and county offices with low reserves, and the department plans to implement our recommendations. However, the department considers our findings and recommendations for the early warning system premature.

INTRODUCTION

California operates a large public school system that serves approximately 4.6 million students in kindergarten through grade twelve (K-12) and over one million students in community colleges throughout the State. The K-12 education system is administered by the State Department of Education (department), 58 county offices of education, and 1,028 school districts. The community colleges are operated by the Board of Governors of the California Community Colleges (board of governors) and 70 locally governed districts.

K-12 Education

The K-12 education system is administered at the state level by the department, under the direction of the State Board of Education and the Superintendent of Public Instruction. The department is responsible for administering and enforcing those powers, duties, and functions that are provided for in the Education Code. For example, the department has specific duties relating to the budgeting and accounting of school districts and county offices of education (county offices). The department also revises and updates budget manuals, forms, and guidelines; cooperates with federal and state agencies in prescribing required regulations and instruction; and conducts training workshops for personnel in the school districts and counties.

The county offices are each operated by a county superintendent of schools in accordance with rules and regulations approved by the county board of education. The superintendent may be elected by the voters in a county or appointed by that county's board of education. The county superintendent of schools is required to distribute all laws, circulars, instructions, and materials for use in the schools and to superintend the school districts, community college districts, and schools operated by the county offices.

Each of the 1,028 school districts in the State is under the control of a separate governing board. School boards have the authority to prescribe and enforce rules as long as these are consistent with the laws established by the Education Code or with the rules prescribed by the State Board of Education. School board members, who are elected officials, appoint a district superintendent of schools. The district superintendent of schools, as the executive officer, is generally responsible for preparing and submitting a budget to the school board and executing the board's policies. The district school board approves and adopts the district budget.

California Community Colleges

The board of governors, which provides statewide leadership for the 70 community college districts, is composed of 15 members: 13 members appointed to four-year terms by the governor with the advice and consent of the Senate, a student member, and a faculty member. The

chancellor of the California community colleges is appointed by the board of governors and is responsible for carrying out the policies of the board of governors.

The community college districts are operated locally by a district chancellor or superintendent in accordance with policies established by the district's governing board of trustees. The district chancellor or superintendent is appointed by the board of trustees and is responsible for preparing and submitting a budget to this board.

Sources of Revenue For Local Educational Agencies

In 1978, the voters of the State passed Proposition 13, which added Article XIII A to the California Constitution, limiting the ability of local educational agencies (LEAs) to levy property taxes. As a result, the State has become increasingly responsible for financing the operations of LEAs. In response to Proposition 13, Chapter 282, Statutes of 1979, and Chapter 1035, Statutes of 1979, were enacted, providing specific levels of state aid for LEAs. Before Proposition 13 was passed, the LEAs received most of their revenue from local sources; since Proposition 13 was passed, the State has provided approximately 65 to 68 percent of the LEAs' revenue. In fiscal year 1986-87, the State will spend approximately \$14 billion on the LEAs. Of this amount, \$13.4 billion will be paid from the State's General

Fund; this represents 43.5 percent of the State's General Fund budget.

Table 1 shows the sources of the LEAs' revenues both before and after Proposition 13.

TABLE 1
EFFECTS OF PROPOSITION 13 (1978)
ON SOURCES OF REVENUE
OF LOCAL EDUCATIONAL AGENCIES

<u>Revenue Source</u>	<u>1977-78 Revenue</u>	<u>Percent</u>	<u>1978-79 Revenue</u>	<u>Percent</u>	<u>1984-85 Revenue</u>	<u>Percent</u>
Federal	\$ 650,384,935	6.9	\$ 698,335,074	7.5	\$ 639,876,828	4.5
Combined federal and state	7,053,764	0.1	6,930,557	0.1	4,061,606	*
State	3,703,317,463	39.1	6,065,054,097	64.8	9,791,408,636	68.3
County	53,594,585	0.5	26,437,729	0.3	19,727,618	0.1
Local						
Property taxes	4,877,494,335	51.5	2,289,868,146	24.5	3,278,681,785	22.9
Sales/rentals and other revenue	<u>180,930,690</u>	<u>1.9</u>	<u>265,275,274</u>	<u>2.8</u>	<u>602,171,826</u>	<u>4.2</u>
Total Revenue	<u>\$9,472,775,772</u>	<u>100.0</u>	<u>\$9,351,900,877</u>	<u>100.0</u>	<u>\$14,335,928,299</u>	<u>100.0</u>

*This revenue source represents less than 0.1 percent of the total revenue.

SCOPE AND METHODOLOGY

The purpose of this audit was to determine the potential magnitude of the financial problems facing the LEAs in the State. We reviewed applicable laws, regulations, and policies governing the department, the board of governors, local school districts, county

offices, and community college districts. We reviewed the department's and the board of governors' analyses of the financial condition of LEAs, and we interviewed personnel at the department, the State Controller's Office, the board of governors, the local school districts, the county offices, and the community college districts. Additionally, we reviewed records at the department and performed tests of compliance with identified policies and procedures.

As part of our review, we analyzed the financial statements of 124 of the 1,156 LEAs in the State. In fiscal year 1985-86, these LEAs represented approximately \$5.5 billion of the \$13.4 billion spent statewide on state education programs and 2.1 million of the 4.9 million in average daily attendance statewide. In addition, we visited eight LEAs, and we prepared projections of their June 30, 1987, general fund balance. Finally, we presented the results of the audit to each of the eight LEAs and considered their comments. Following is a list of the LEAs we visited and their average daily attendance for fiscal year 1985-86.

<u>Local Educational Agency</u>	<u>1985-86 Average Daily Attendance</u>	<u>County</u>
Peralta Community College District	14,729	Alameda
Alameda County Office Of Education	656	Alameda
Chaffey Joint Union High School District	14,442	San Bernardino
Fullerton School District	9,476	Orange
Oakland Unified School District	49,152	Alameda
Richmond Unified School District	27,499	Contra Costa
Santa Monica-Malibu Unified School District	9,347	Los Angeles
Ukiah Unified School District	6,100	Mendocino

To determine the financial condition of the State's LEAs, we analyzed a sample of 124 LEAs. Using the LEAs' average daily attendance figure for the 1985-86 fiscal year, we categorized them as either large, medium, or small. In addition, the representation of school districts, county offices, and community college districts in our sample approximates their representation in the total population. Table 2 shows the number of LEAs we reviewed in each category.

TABLE 2
124 LOCAL EDUCATIONAL AGENCIES
BY CATEGORY AND AVERAGE DAILY ATTENDANCE

<u>Local Educational Agency</u>	<u>Size By Average Daily Attendance</u>			<u>Total</u>
	<u>Small</u>	<u>Medium</u>	<u>Large</u>	
School districts	30 (1--1,000)	33 (1,001-15,000)	48 (15,001+)	111
County offices of education	1 (1--1,000)	2 (1,001-5,000)	3 (5,001+)	6
Community college districts	1 (1--10,000)	3 (10,001-25,000)	3 (25,001+)	<u>7</u>
Total	<u>32</u>	<u>38</u>	<u>54</u>	<u>124</u>

Of the 124 LEAs we selected, the 54 large LEAs represent 39 percent of the State's total Average Daily Attendance (ADA), the 38 medium LEAs represent 4 percent of the State's total ADA, and the 32 small LEAs represent less than one percent of the State's total ADA.

We reviewed each of the 124 LEAs' audited financial statements for the fiscal year ended June 30, 1986. Specifically, we analyzed the LEAs' general fund balances and their current revenues and expenditures. To calculate each LEA's fund balance at June 30, 1986, we totaled the balances of the LEA's unreserved accounts and its accounts not reserved for specific purposes; these balances were stated on the LEA's audited June 30, 1986, financial statements. In addition, we reduced the fund balance for amounts that, in our judgment, should have been reserved (such as amounts for inventory) and for amounts owed to the LEA that may not be collectible. Finally, we increased the fund balance if the LEA had established a reserve for California State Lottery revenue. We also reviewed the 124 LEAs' budgetary information for the 1985-86 fiscal year and their ADA for five fiscal years, 1981-82 through 1985-86.

For each of the 124 LEAs, we calculated a ratio of fund balance to expenditures: we divided its fund balance as of June 30, 1986, by expenditures for the 1985-86 fiscal year. We also calculated a ratio of revenues to expenditures: we divided its 1985-86 fiscal year revenues by 1985-86 fiscal year expenditures. We used these two calculations to determine the LEAs that have a low or nonexistent fund balance compared to their expenditures and to determine the LEAs whose expenditures exceeded their revenues for the 1985-86 fiscal year. Based on the results of these two calculations, we selected the 25 LEAs with the lowest fund balance-to-expenditure ratios (excluding California State Lottery funds) and the lowest

revenue-to-expenditure ratio and obtained their audited financial statements for the fiscal years 1983-84 and 1984-85. We performed additional analyses of their fund balances, revenues, expenditures, and budgetary data to determine if these LEAs are facing possible financial problems.

In conducting this review, we relied on financial information provided by the LEAs, their auditors, the department, and the board of governors. Because the procedures above were not sufficient to constitute a separate examination made in accordance with generally accepted auditing standards, we do not express an opinion on any of the financial statements referred to in this report.

AUDIT RESULTS

I

MANY SCHOOL DISTRICTS, COUNTY OFFICES OF EDUCATION, AND COMMUNITY COLLEGE DISTRICTS ARE FACING FINANCIAL PROBLEMS

Many local educational agencies (LEAs)--school districts, county offices of education (county offices), and community college districts--have low financial reserves and continually spend more than they receive in revenue. As a result of this trend, since fiscal year 1981-82 the State has approved emergency loans totaling \$23.9 million to 12 LEAs. LEAs have had these financial problems because they base their budgets on inaccurate estimates of revenue and expenditures, because they use general fund monies to pay for overspending in other funds, or because they have granted salary increases that are larger than the increases in the revenues used to pay for salaries. Excessive administrative costs and declining attendance have also contributed to the financial problems of some LEAs.

To determine the financial condition of the State's LEAs, we selected a sample of 124 LEAs and analyzed their audited financial statements for fiscal year 1985-86. From the 124 LEAs, we selected 25 LEAs that either had a deficit or a low fund balance or displayed other conditions that indicate a poor financial condition, and we analyzed their spending patterns between fiscal years 1983-84 and 1985-86. Finally, to determine the causes of the financial problems that are

facing LEAs, we visited an additional 8 LEAs. We selected 5 of these LEAs because the State Department of Education (department) had identified them as likely to require financial assistance, and we selected 3 LEAs that we had audited before because of their financial problems.

Analysis of 124 Local Educational Agencies

As of June 30, 1986, 25 of the 124 LEAs we reviewed had low fund balances;* in fact, at June 30, 1986, the fund balances of 3 of these LEAs showed a total deficit of approximately \$899,000. Furthermore, 25 of the LEAs that we examined allowed expenditures to exceed their revenues during fiscal year 1985-86. Finally, up to 23 of these LEAs may have deficit fund balances totaling approximately \$28 million as of June 30, 1987, if they continue to spend more than they receive in revenues.

Analysis of Fund Balances

The fund balance represents the difference between an LEA's assets and its liabilities. From year to year, the fund balance will

*We calculated the ratio of fund balance to expenditures for all LEAs of a similar size and averaged these ratios. We determined that an LEA's fund balance was low if its fund balance-to-expenditures ratio was in the lowest 25 percent of the averaged ratios.

change: it will increase if the LEA's revenues exceeded its expenditures, and it will decrease if its expenditures exceeded its revenues. The fund balance at the end of a fiscal year can be used to measure the ability of an LEA to fund a portion of its operations for the succeeding fiscal year if economic conditions cause expenditures to exceed revenues or if revenues simply do not meet anticipated levels and the LEA does not reduce planned expenditures.

In determining the fund balance for the 124 LEAs, we made adjustments for amounts owed to the LEA's general fund that may not be collected. Specifically, we adjusted 4 of the 124 LEAs' fund balances totaling \$384,261 for amounts owed to the LEAs' general fund by one of its other funds because these other funds had deficit or insufficient fund balances as of June 30, 1986.

As of June 30, 1986, 25 of the 124 LEAs we examined had low fund balances, and 3 of the LEAs had deficit fund balances that totaled approximately \$899,000. Furthermore, 11 of 25 LEAs with low fund balances spent more than they received in revenue in at least two of the last three fiscal years. For example, one school district has reduced its fund balance approximately \$2.5 million between fiscal years 1983-84 and 1985-86. (See Appendix A for graphs and tables showing the ratio of fund balance to expenditures at June 30, 1986, for the 124 LEAs we reviewed.)

Currently, there is no required minimum fund balance that an LEA must maintain, and a low or negative fund balance is not necessarily an indicator of immediate financial difficulty. However, an LEA with a low or negative fund balance does not have a safety margin that could help it avoid seeking additional state funding if conditions cause the LEA's expenditures to significantly exceed its revenues.

Analysis of Revenues and Expenditures

In 99 of the 124 LEAs we reviewed, revenues exceeded expenditures by a margin of \$2,171 to \$50 million in fiscal year 1985-86. However, in the remaining 25 LEAs', expenditures exceeded revenues by a margin of \$2,366 to \$2.6 million. In addition, the LEA whose expenditures exceeded its revenues by \$2.6 million ended the fiscal year with a low fund balance of \$164,868. (Appendix B shows the 124 LEAs' expenditures and revenues for fiscal year 1985-86 and the LEAs' fund balance at June 30, 1986.)

In addition, in 13 of our sample of 25 LEAs that we determined face possible financial problems, expenditures exceeded revenues during two out of the last three fiscal years, and in one of these LEAs, expenditures had exceeded revenues in three of the last three fiscal years. In addition, one of these 3 LEAs had a deficit fund balance of \$660 as of June 30, 1986. Table 3 shows the effects of deficit spending on these 25 LEAs between fiscal years 1983-84 and 1985-86.

TABLE 3
EFFECTS OF DEFICIT SPENDING
25 LOCAL EDUCATIONAL AGENCIES
FISCAL YEARS 1983-84 THROUGH 1985-86

Local Educational Agency	Fiscal Years With Deficit Spending			Overall Change in Fund Balance 1983-84 to 1985-86	Ending Fund Balance 6/30/86	Fiscal Year 1985-86 Expenditures	Ratio of Fund Balance to Expenditures
	1983- 1984	1984- 1985	1985- 1986				
Coast Community College		X	X	\$ (156,771)	\$ 164,868	\$ 89,020,367	0.19%
Contra Costa Community College		X	X	\$ 1,697,308	\$3,323,574	\$ 55,475,806	5.99%
Los Angeles Community College		X		\$ (231,775)	\$7,778,583	\$193,832,900	4.01%
San Diego Community College	X	X		\$ 1,509,000	\$3,483,000	\$ 71,940,000	4.84%
Santa Monica Community College	X	X		\$ 445,257	\$1,878,375	\$ 32,248,948	5.82%
ABC Unified		X		\$ (1,279,822)	\$4,074,686	\$ 74,239,099	5.49%
Albany Unified	X	X		\$ (33,904)	\$ 160,333	\$ 8,098,679	1.98%
Amador Valley Joint Union High	X		X	\$ 358,682	\$ 508,770	\$ 15,567,413	3.27%
Arcadia Unified		X		\$ 347,126	\$1,166,416	\$ 22,530,660	5.18%
Beaumont Unified	X	X		\$ 207,999	\$ 272,741	\$ 8,048,439	3.39%
Conejo Valley Unified				\$ 2,360,410	\$2,793,886	\$ 54,441,219	5.13%
Fontana Unified				\$ 1,462,035	\$2,561,035	\$ 46,855,367	5.47%
Friant Union	X	X	X	\$ (45,259)	\$ (660)	\$ 306,977	-0.21%
Guerneville Elementary		X		\$ (99,383)	\$ 64,343	\$ 1,759,871	3.66%
Hayward Unified	X	X		\$ (390,475)	\$2,217,924	\$ 54,350,184	4.08%
Newport-Mesa Unified		X	X	\$ (1,575,917)	\$ (833,509)	\$ 71,710,027	-1.16%
Rim of the World Unified	X		X	\$ (103,061)	\$ 131,027	\$ 14,958,521	0.88%
Riverside Unified				\$ (292,075)	\$3,096,607	\$ 76,100,400	4.07%
Sacramento City Unified		X	X	\$ (2,556,293)	\$2,546,210	\$144,520,184	1.76%
San Francisco Unified	X			\$ 2,676,300	\$5,548,309	\$195,721,177	2.83%
San Mateo County Office		X		\$ 157,049	\$ 157,049	\$ 33,121,639	0.47%
Santa Rosa Elementary	X	X		\$ (56,565)	\$ (65,254)	\$ 11,485,599	-0.57%
Union Hill	X	X		\$ 4,636	\$ 24,547	\$ 807,982	3.04%
William S. Hart Union High		X		\$ 1,072	\$ 830,955	\$ 33,241,163	2.50%
Windsor Union	—	X	—	\$ (123,143)	\$ 67,652	\$ 3,013,180	2.25%
Totals	<u>11</u>	<u>19</u>	<u>7</u>				

As Table 3 shows, 8 LEAs had deficit spending in one of the three fiscal years, 13 LEAs had deficit spending in two of the three fiscal years, and one had deficit spending in all three of the fiscal years. The decrease in the number of LEAs that had deficit spending in fiscal year 1985-86 compared to fiscal year 1984-85 corresponds to the first year the LEAs received revenues from the California State Lottery.

Fund Balance Projection

To determine the effect of greater expenditures than revenues on the fund balances of the 124 LEAs we examined, we projected the fund balances to June 30, 1987. To calculate this projection, we made several assumptions based on our analysis of the 25 LEAs that we determined face possible financial problems. Since the expenditures for these 25 LEAs exceeded their revenues by an average of 3 percent, we projected, for fiscal year 1986-87, an increase in expenditures of 3 percent over fiscal year 1985-86 expenditures, and we projected revenues that would remain constant at fiscal year 1985-86 levels.* We

*Although, for ease of calculation, we assumed that revenue would remain constant while expenditures increase, we realize that this will not normally be the case. However, our method results in essentially the same fund balance as if we had increased both expenditures and revenue. For example, an increase of 3 percent in expenditures, with no increase in revenue, is roughly equivalent to an increase of 4 percent in expenditures and an increase of one percent in revenue.

performed the same projection using increases of 2 percent, 4 percent, and 5 percent over the LEAs' 1985-86 expenditures and holding revenues constant at fiscal year 1985-86 levels. Table 4 shows the results of our projections.

TABLE 4
RATIO OF FUND BALANCE TO EXPENDITURES
PROJECTED TO JUNE 30, 1987
FOR 124 LOCAL EDUCATIONAL AGENCIES

<u>Projected Increase in Expenditures</u>	<u>Ratio of Fund Balance to Expenditures</u>		
	<u>Less Than 0</u>	<u>Between 0 and 3</u>	<u>Greater Than 3</u>
2 Percent	9 LEAs	14 LEAs	101 LEAs
3 Percent	12 LEAs	19 LEAs	93 LEAs
4 Percent	17 LEAs	16 LEAs	91 LEAs
5 Percent	23 LEAs	21 LEAs	80 LEAs

If expenditures continue to exceed revenues by 3 percent, as many as 12 LEAs will have deficit fund balances totaling approximately \$16.6 million at June 30, 1987. If expenditures exceed revenues by as much as 5 percent, as many as 23 LEAs will have deficit fund balances totaling approximately \$28 million at June 30, 1987. In addition, at increases of 2 percent, 9 LEAs will have deficit fund balances totaling \$12.2 million, and at 4 percent, 17 LEAs will have deficit fund balances totaling \$21.7 million.

Average Daily Attendance

The Average Daily Attendance (ADA) of 8 of the 25 LEAs that we determined may face possible financial trouble decreased between fiscal year 1981-82 and fiscal year 1985-86; however, their expenditures have increased over the same period. For example, one LEA's ADA has decreased 25.9 percent (from 35,566 to 26,323), and its expenditures have increased approximately \$14.3 million during the same period. Although the overall ADA of all 124 LEAs increased only 3.31 percent between fiscal years 1981-82 and 1985-86, the ADA for certain LEAs fluctuated greatly, especially the community college districts, whose ADA decreased dramatically. For example, the ADA for one school district increased by 45.9 percent while the ADA for another school district decreased 33.05 percent. However, the ADA for all of the community college districts in our sample decreased during the five-fiscal year period, from a total of 201,854 ADA in fiscal year 1981-82 to a total of 155,161 ADA in fiscal year 1985-86. Table 5 shows the percent of change in the ADA of the 124 LEAs between fiscal years 1981-82 and 1985-86. (See Appendix C for a detailed summary of the ADA of the LEAs during this period.)

TABLE 5
CHANGE IN AVERAGE DAILY ATTENDANCE
IN 124 LOCAL EDUCATIONAL AGENCIES
BETWEEN FISCAL YEARS 1981-82 AND 1985-86

Type of LEA	Decrease							Increase						
	More Than -25%	-20% to -25%	-15% to -20%	-10% to -15%	-5% to -10%	0% to -5%	Total	5% to 0%	10% to 5%	15% to 10%	20% to 15%	25% to 20%	More Than 25%	Total
Community College	2	0	1	2	2	0	7	0	0	0	0	0	0	0
K-12														
Small LEA	1	0	2	2	5	2	12	5	3	2	0	1	7	18
Medium LEA	1	0	0	1	5	5	12	5	5	9	1	0	1	21
Large LEA	0	0	1	0	5	6	12	12	7	12	2	3	0	36
County Office of Education	0	0	0	0	0	1	1	0	0	1	2	1	1	5
Totals	<u>4</u>	<u>0</u>	<u>4</u>	<u>5</u>	<u>17</u>	<u>14</u>	<u>44</u> (35%)	<u>22</u>	<u>15</u>	<u>24</u>	<u>5</u>	<u>5</u>	<u>9</u>	<u>80</u> (65%)

Budget Analysis

We were unable to determine the adequacy of the 124 LEAs' proposed fiscal year 1985-86 budget because the LEAs did not include in their budgets revenue from the California State Lottery because of the apparent uncertainty of the amounts the LEAs would receive. However, because the LEAs received and spent lottery revenue during the fiscal year 1985-86, our comparison of the LEAs' proposed budgets and their actual expenditures and revenues would show significant variances, and the results would be inconclusive.

Seven of the Eight Local
Educational Agencies We Visited
Are Facing Financial Problems

According to the Education Code, it is the intent of the Legislature to encourage sound fiscal management practices and fiscal accountability among local LEAs so that they can most effectively and efficiently use public funds to educate children and community college students in California. However, since fiscal year 1981-82, 12 LEAs have had financial problems that have required the State to approve loans totaling \$23.9 million. One school district, which received a loan in fiscal year 1982-83, is requesting a second loan of \$500,000 for fiscal year 1987-88. To determine why LEAs are experiencing financial problems, we visited eight of them. We selected five LEAs from those identified by the department as likely to require financial assistance. In addition, we selected three LEAs that we had previously audited because of their financial problems. Our sample consisted of six school districts (one high school district, one elementary school district, and four unified school districts); one county office; and one community college district. In addition, we selected LEAs serving rural, urban, and suburban areas in five counties throughout the State.

Seven of the eight LEAs that we visited are facing financial problems. Six of them had low fund balances in fiscal year 1985-86, and four spent more than they received in revenue in at least three of the last four fiscal years. We project that, unless the LEAs are able

to increase their revenues or reduce their expenditures, six of the eight LEAs we visited will end fiscal year 1986-87 with a general fund deficit.

The seven LEAs' general fund balances have declined for a variety of reasons. Seven LEAs used inaccurate estimates of revenue and expenditures to prepare their budgets, and seven used general fund monies to pay for overspending in other funds. In addition, the seven LEAs have granted salary increases that are larger than the increases in the revenue used to pay the salaries. Finally, excessive administrative costs and declining attendance have contributed to the decreasing fund balance of four of the LEAs.

According to the audited financial statements, in their general fund budgets for three of the last four fiscal years, six of the eight LEAs budgeted expenditures that were greater than the revenue they expected to receive. The remaining two LEAs budgeted expenditures that were greater than their expected revenue in each of the last four fiscal years. Budgeting for expenditures that exceed revenue may be an acceptable budgeting practice provided the LEAs maintain an adequate fund balance. However, since this practice reduces the fund balance, it depletes resources that could be used to withstand possible adverse conditions in the future. As a result of this method of budgeting, between June 30, 1982, and June 30, 1986, all eight LEAs reduced their general fund balance in at least two of these four years, as the following table shows.

TABLE 6

**AUDITED ENDING FUND BALANCES
EIGHT LOCAL EDUCATIONAL AGENCIES
FISCAL YEARS 1981-82 THROUGH 1985-86**

Local Educational Agency	Fiscal Year				
	1981-82	1982-83	1983-84	1984-85	1985-86*
Peralta CCD	\$ 417,549	\$ (452,168)	\$ (931,445)	\$ (5,056,681)	\$ (5,763,513)
Alameda COE	\$ 885,585	\$ (369,714)	\$ (5,754,804)	\$ 363,204	\$ 1,430,092
Chaffey HSD	\$1,096,947	\$1,070,390	\$ 669,422	\$ 371,984	\$ 1,036,257
Fullerton SD	\$2,359,744	\$2,038,050	\$ 1,492,778	\$ 118,558	\$ 314,032
Oakland USD	\$ (494,363)	\$ (739,652)	\$ (747,030)	\$ (1,619,330)	\$ 603,140
Richmond USD	\$ (18,243)	\$1,589,783	\$ 736,591	\$ (271,444)	\$ 3,353,111
Santa Monica- Malibu USD	\$2,356,781	\$ 770,301	\$ 618,215	\$ (188,502)	\$ (453,605)
Ukiah USD	\$1,518,059	\$ 290,462	\$ (316,508)	\$ (172,483)	\$ 778,312

*Fiscal year 1985-86 was the first year that local educational agencies received revenue from the California State Lottery.

CCD = Community College District
COE = County Office of Education
HSD = High School District
SD = School District
USD = Unified School District

Both Peralta Community College District and Santa Monica-Malibu Unified School District reduced their general fund balances in each of the four years from approximately \$418,000 and \$2,357,000, respectively, in fiscal year 1981-82 to deficit fund balances of approximately \$5,764,000 and \$454,000, respectively, in fiscal year 1985-86. The increase in the fund balance for six of the eight LEAs in fiscal year 1985-86 corresponds to the first year the LEAs received revenues from the California State Lottery.

As Table 7 shows, we are projecting that six of the eight LEAs we visited will have general fund deficits in fiscal year 1986-87. (Appendix D lists the assumptions we used to prepare the fund balance projections.)

TABLE 7

FUND BALANCE FORECASTS FOR JUNE 30, 1987
EIGHT LOCAL EDUCATIONAL AGENCIES

	Peralta Community College	Alameda Co. Office of Education	Chaffey Joint Union High	Fullerton	Oakland Unified	Richmond Unified	Santa Monica Malibu Unified	Ukiah Unified
Sources								
Federal revenue	\$ 3,616,000	\$ 382,000	\$ 730,000	\$ 1,049,000	\$ 12,469,000	\$ 4,735,000	\$ 1,941,000	\$ 503,000
Combined federal and state	0	0	0	0	84,000	0	0	0
State revenue	36,373,000	7,558,000	34,812,000	17,327,000	145,282,000	64,346,000	22,539,000	12,232,000
State lottery income	1,267,000	52,000	1,363,000	894,000	4,139,000	2,342,000	868,000	500,000
County & local income	8,990,000	4,356,000	12,974,000	11,002,000	23,713,000	22,736,000	14,136,000	5,710,000
Transfers from other funds	0	0	934,000	146,000	8,000	0	320,000	1,754,000
Total Sources	50,246,000*	12,348,000	50,813,000	30,418,000	185,695,000	94,159,000	39,804,000	20,699,000
Uses								
Certificated salaries	21,222,000	2,664,000	25,463,000	15,725,000	92,183,000	50,861,000	19,923,000	10,225,000
Classified salaries	11,833,000	2,959,000	7,251,000	5,744,000	31,145,000	17,475,000	6,651,000	3,065,000
Employee benefits	6,971,000	1,572,000	7,846,000	5,043,000	34,936,000	16,209,000	6,687,000	3,165,000
Books and supplies	1,156,000	1,242,000	1,937,000	1,497,000	8,230,000	3,028,000	1,466,000	860,000
Contracted services	7,604,000	2,569,000	3,142,000	1,699,000	16,842,000	8,114,000	3,127,000	1,450,000
Capital outlay	1,250,000	1,249,000	1,455,000	358,000	2,030,000	1,037,000	541,000	585,000
Other	1,433,000	18,000	2,745,000	367,000	5,276,000	2,208,000	634,000	2,189,000
Total Uses	51,469,000	12,273,000	49,839,000	30,433,000	190,642,000	98,932,000	39,029,000	21,539,000
Appropriation for Contingencies	290,000	555,000	2,070,000	216,000	0	0	557,000	316,000
Forecasted Net Increase (Decrease)								
In Fund Balance for Fiscal Year 1986-87	(1,513,000)	(480,000)	(1,096,000)	(231,000)	(4,947,000)	(4,773,000)	218,000	(1,156,000)
Beginning Fund Balance at July 1, 1986, as Restated	(5,022,000)	1,440,000	1,209,000	496,000	4,106,000	3,897,000	(222,000)	874,000
Prior Period Adjustment	0	0	0	0	(920,000)	0	0	0
Fund Balance Forecast for June 30, 1987	(6,535,000)	960,000	113,000	265,000	(1,761,000)	(876,000)	(4,000)	(282,000)
Reserved for inventory	222,000	0	140,000	180,000	1,000,000	200,000	180,000	74,000
Reserved for prepaid expenses	500,000	0	0	0	0	0	0	18,000
Reserved for revolving fund cash	19,000	10,000	25,000	20,000	65,000	20,000	40,000	4,000
Unreserved Fund Balance Forecast for June 30, 1987	\$(7,276,000)	\$ 950,000	\$ (52,000)	\$ 65,000	\$ (2,826,000)	\$(1,096,000)	\$ (224,000)	\$ (378,000)

*Total sources do not include a possible emergency apportionment of \$3.3 million. (See Appendix D.)

Reasons for the LEAs' Financial Problems

Our review of the expenditures and revenues of the eight LEAs for the current fiscal year and the past four fiscal years identified some of the reasons that their expenditures have exceeded revenues. We attempted to identify those problems that are similar among the LEAs as well as those that seem to be specific to each LEA. No single factor should be considered the primary or exclusive cause of an LEA's financial difficulties. Instead, each factor should be considered one of many contributing factors.

Difficulties in Preparing Budget Estimates

Seven of the eight LEAs we reviewed have had problems in budgeting revenues. The LEAs find it difficult to accurately budget for state apportionments when revenues are based upon an estimate of their average daily attendance (ADA). To estimate ADA, an LEA uses its knowledge of its history of either declining or increasing ADA, the effects of the high school dropout rate, and other factors specific to its situation. Approximately seven months into each fiscal year, the LEA revises its ADA to reflect "actual" ADA. The ADA is revised a second time approximately 11 months into the fiscal year. If the revised, actual ADA is less than originally estimated, the LEA will receive less revenue than it originally budgeted for.

For example, one LEA's revised actual ADA for fiscal year 1986-87 was approximately 2 percent less than it originally estimated. This decrease in its ADA will result in a corresponding reduction of approximately \$3.2 million in its state revenues for fiscal year 1986-87. However, this may not be the final amount of state revenues the district will receive because the ADA will be revised one more time during the current fiscal year.

Another variable factor LEAs must deal with is the budgeting of California State Lottery revenue. In preparing their budget for fiscal year 1986-87, six of the LEAs used estimates of lottery revenues based on prior year's actual revenues, or they used estimates provided by outside consultants. Since these estimates differed significantly from the most current estimate of amounts to be received, these LEAs were required to make significant reductions in budgeted revenues and expenditures.

For example, one LEA initially obtained from a private consultant an estimate of \$125 per ADA in California State Lottery revenues. However, in fiscal year 1985-86, this LEA's estimates of lottery revenues had been understated by 15 percent. Therefore, with the approval of the LEA's board of trustees and its county office of education, the LEA used \$157 per ADA as an estimate of lottery revenues when preparing its fiscal year 1986-87 budget, believing that lottery revenues would again exceed expectations in the current year. However, the latest estimate of lottery revenue provided by the private

consultant is \$86 per ADA; therefore, this LEA has had to cut \$71 per ADA, a total of approximately \$676,000, from its initial 1986-87 budget. Although the LEA had tentative plans for spending lottery revenues of \$157 per ADA, it did not allocate the lottery reserve to specific expenditures and did not enter into purchase agreements until it was certain that it would receive the revenue.

Another LEA budgeted fiscal year 1986-87 lottery revenue at \$125 per ADA. The LEA was not aware that estimated lottery revenues were later reduced to approximately \$86 per ADA because the LEA did not subscribe to newsletters from outside consultants. In addition, although the board of governors was aware of the decline in estimated lottery revenues, it failed to notify the LEA because it wanted to be assured that the decline in estimated lottery revenues would actually occur.

LEAs' Expenditures Have Exceeded Revenues In Some Programs

In seven of the eight LEAs we visited, expenditures exceeded revenues in various programs traditionally funded by sources other than the general fund. As a result, general fund monies have been used and will be used in fiscal year 1986-87 to fund these activities that are not normally funded by the general fund.

For example, in recent years, the expenditures of the child development programs in three LEAs have consistently exceeded the

programs' revenues, and these LEAs have had to transfer general fund monies to their child development funds. The expenditures of one LEA's child development fund have exceeded its revenues for three of the last four years, and its expenditures are projected to exceed its revenues in the current fiscal year as well. As a result, the general fund has paid to this LEA's child development fund approximately \$194,000 to \$826,000 between fiscal years 1982-83 and 1985-86. In the current year, the LEA is projecting that its child development fund will need approximately \$78,000 in general fund monies. Another LEA is estimating that its child development fund will require approximately \$360,000 of general fund monies in the current fiscal year.

The cafeteria fund expenditures for five of the LEAs have exceeded their revenues in recent years. As shown in Table 8, the general funds will have paid the cafeteria funds of these LEAs between approximately \$41,700 and \$194,200 in the past four fiscal years. These amounts do not include indirect subsidies, such as charging the general fund rather than the cafeteria fund for its utilities.

TABLE 8

**TRANSFERS FROM THE GENERAL FUNDS TO THE CAFETERIA FUNDS
OF FIVE LOCAL EDUCATIONAL AGENCIES
FISCAL YEARS 1983-84 THROUGH 1986-87**

<u>Local Educational Agencies</u>	<u>Fiscal Year</u>			
	<u>1983-84</u>	<u>1984-85</u>	<u>1985-86</u>	<u>1986-87</u>
Santa Monica-Malibu Unified School District	\$ 0	\$194,187	\$ 0	\$ 0
Fullerton School District	\$ 0	\$ 0	\$ 0	\$ 41,657*
Richmond Unified School District	\$ 0	\$ 0	\$120,852	\$ 96,000**
Chaffey Joint Union High School District	\$51,578	\$ 67,770	\$100,000	\$101,320**
Ukiah Unified School District	\$ 0	\$ 0	\$135,587	\$ 99,695***

*The Fullerton School District anticipates transferring this amount in the current fiscal year. However, this amount actually represents the combination of the cafeteria losses in fiscal years 1984-85 and 1985-86.

**Projected amount to be transferred.

***The Ukiah Unified School District has transferred this amount as of January 12, 1987. Additional funds may be transferred during the remaining portion of the year, if needed.

Officials of three of the eight LEAs we visited believe that their special education programs are not fully funded and that they need to use monies from the general fund allocated to regular classroom instruction to pay for the underfunded portion. For example, one LEA has calculated that its special education program was underfunded by \$3.6 million in fiscal year 1981-82, and the amount of underfunding has steadily increased to \$4.6 million in fiscal year 1985-86.

The department acknowledges that there seem to be various problems in the funding structure of special education programs that could leave a portion of some LEAs' special education programs unfunded. For example, 11.6 percent of one LEA's total student enrollment participates in the special education program. Since the State will pay only 10 percent of total enrollment for special education, the funding of the additional 1.6 percent, which represents 460 special education pupils, comes from other general fund sources. According to department officials, another problem with the State's funding of the special education program is that it uses fiscal year 1978-79 as a base year; if an LEA's special education program costs for that year were low, the program will receive low funding now. According to one LEA's officials, its base year costs were much lower than the statewide average; as a result, funding for its special education program continues to be lower than the amount it needs.

The 1986-87 Budget Act required the department to establish a special education task force. The task force is attempting to develop a new special education funding formula that plans to provide the LEAs with sufficient special education funding. The task force plans to propose the new funding formula to the Department of Finance for its approval by November 15, 1987.

Finally, one LEA's unrestricted general fund monies are subsidizing restricted funds, which represent revenues from grants and contracts that must be spent for a specific purpose. If this

restricted revenue is not received or is inadequate to match the expenditures incurred, transfers are made from the general fund's unrestricted funds. In fiscal year 1984-85, the LEA entered into several state contracts that required students to complete a training program and be placed in a job. Because many students were not placed in a job, the LEA lost approximately \$1.4 million in income. Although the LEA no longer enters into these contracts, the program continues to incur expenditures that exceed its revenue from existing grants and contracts. In fiscal year 1986-87, the LEA estimates that the unrestricted General Fund transfer for this program will be approximately \$657,000.

Salary Increases Exceed Program Increases

Another cause of the LEAs' financial difficulties is that LEAs are granting their employees salary increases that exceed the increases in the revenues of various state and federal programs. The problem is compounded because LEAs typically give all of their employees the same salary increase, but the state and federal governments do not grant the same increases to the programs that fund employee salaries. Between fiscal years 1982-83 and 1985-86, five of the LEAs we reviewed authorized total increases in teacher salaries that were greater than the total increases in the state revenue limit, the major source of revenue for regular classroom instruction. For example, one LEA granted its teachers a total salary increase of 26 percent for the last four fiscal years; however, the State's revenue limit increased only

20.21 percent during these same four years. Six of the eight LEAs have settled their negotiations for the current fiscal year and have granted teacher salary increases that are greater than the 5.49 percent and 5.77 percent increases in the revenue limit for school districts and community college districts, respectively. For example, one LEA granted a 9.58 percent increase.

In addition, four of the six LEAs that receive child nutrition funding for their cafeteria fund have granted cafeteria employees total salary increases that are greater than the increases the federal government has given the child nutrition program. For example, between fiscal years 1982-83 and 1985-86, one LEA has granted its cafeteria employees a total salary increase of 26 percent when funding for the child nutrition program has increased only 17.80 percent during the same period. Five of the six LEAs have settled their negotiations for fiscal year 1986-87 and continued to grant salary increases that are greater than the increase of 4.0 percent granted to the child nutrition program. For example, one LEA has granted a salary increase of 9.58 percent.

Additionally, six LEAs granted total salary increases that are greater than the child development program's total revenue increases for fiscal years 1982-83 through 1985-86. For example, one LEA granted a total salary increase of 26 percent over the past four years while the State's funding of the child development program increased only 14 percent. Five of the LEAs have settled their negotiations for

fiscal year 1986-87, and they have all granted salary increases that are greater than the child development program's increase of one percent. For example, one LEA has granted a 9.58 percent salary increase.

Excessive Administrative Costs

The Education Code, Section 41402, establishes ratios of administrators to teachers that school districts must meet. For every 100 teachers requiring certificates, a unified school district may employ no more than 8 administrators in positions that require certificates. An elementary and high school district may hire no more than 9 and 7 administrators per 100 teachers, respectively. The California Basic Educational Data System (CBEDS), a unit of the department, reported that, in October 1985, 200 out of the 1,028 school districts within the State exceeded their administrator limit. Of these 200, 25 were exempt from compliance, and 6 requested waivers. All but one of the 169 remaining LEAs submitted certifications that the initial data sent to CBEDS was incorrect and that they were actually within the required administrator limit. However, according to our review, the accuracy of the LEAs' certifications may be questionable.

To determine whether they spent too much of their funds on administrative salaries, we reviewed the ratio of administrators to

teachers in five school districts for fiscal year 1985-86.* Three of the five LEAs exceeded the limits set by the Education Code, Section 41402, and, therefore, spent too much of their funds on administrative salaries. These three LEAs were among those that had certified that they were within the required administrator limit.

One LEA exceeded its administrator limit by 44 administrators, which would have resulted in an approximate \$1.7 million reduction in funding, if a reduction had been imposed. As calculated by the Education Code, Section 41404, this reduction in funding represents the state funds that were used by the LEA to pay the excess administrator salaries. The remaining two LEAs exceeded their administrator limits because the LEAs and their employees incorrectly interpreted the department's instructions, issued in October 1985, regarding employee classifications. In addition, because the department's instructions were inconsistent and did not clearly indicate whether employees in adult education and child development programs should be included in the calculation of the administrator limit, these employees did not report to the department. When the employees were correctly classified in accordance with interpretations by the department and the adult

*We did not review the administrator-to-teacher ratio at one LEA because data submitted by the teachers and administrators indicated that this district was well within the limit established by the Education Code. We did not review the administrator-to-teacher ratio at the two remaining LEAs because the ratio is not applicable to county offices or community college districts.

education and child development employees were included, we found that the two LEAs had exceeded their limits by 5 administrators in one instance and 9 in the other.

Declines In Average Daily Attendance
May Add to an LEA's Financial Difficulties

Three of the LEAs we reviewed have experienced significant decreases in their average daily attendance (ADA) over the last few years. Since ADA is used to calculate the major portion of an LEA's state funding, these LEAs have had a corresponding decrease in their state revenues. According to LEA officials, the decrease in revenue is a cause of many of their financial difficulties. In theory, if revenue decreases, the LEA should decrease its expenditures by a corresponding amount; however, because of pressure from teachers, parents, and students, this is not always possible.

For example, in one LEA, the ADA decreased by approximately 12,000 between fiscal years 1971-72 and 1980-81 and continued to decrease by approximately 1,500 ADA through fiscal year 1984-85. Even though the major decrease in ADA occurred in the earlier years, the LEA's officials did not begin closing schools until 1981. The majority of school closures occurred in 1983, when the LEA's financial situation became critical. According to the LEA's officials, the delay in school closures occurred because, between 1971 to 1980, the LEA's board of education believed that neighborhood schools should exist at any cost.

Future Outlook

We project that six of the eight LEAs will end fiscal year 1986-87 with a general fund deficit and, therefore, will face financial problems in fiscal year 1987-88. In addition, five of these LEAs will begin the process of negotiating salary increases for fiscal year 1987-88; in the past, these salary increases have generally exceeded 4 percent. The sixth LEA is already committed to a multi-year contract granting its teachers a 7 percent salary increase in fiscal year 1987-88. The 7 percent increase does not include the step increases the LEA automatically gives for seniority and additional training.

To pay for their fiscal year 1986-87 general fund deficits and any negotiated salary increases, most of the LEAs we reviewed will require more than the 2.2 and 2.7 percent increases that the governor has proposed to the major source of state funds for school districts and community college districts, respectively. Since these increases are effective January 1, 1988, the school districts and community college districts will actually receive increases for the 1987-88 school year of only 1.1 percent and 1.35 percent, respectively. In addition, the governor does not plan to fund the Urban Impact and Meade Aid programs in fiscal year 1987-88. As a result of the loss of the Urban Impact and Meade Aid revenues, the 2.2 percent and 2.7 percent increases, and negotiated salary increases, most of these LEAs will have to make drastic reductions in their expenditures just to maintain their present financial condition. For example, we estimate that, if

the LEAs receive the state funds as the governor has proposed, one LEA will have to find additional cost savings of between approximately \$7.0 million and \$13.5 million (4 to 7.5 percent of its fiscal year 1986-87 budget) to meet its salary commitments and to recover from its fiscal year 1986-87 projected deficit.

CONCLUSION

Many local educational agencies have low fund balances and continually spend more than they receive in revenue. As a result of this trend, since fiscal year 1981-82 the State has approved emergency loans totaling \$23.9 million to 12 local educational agencies. These problems have occurred because some LEAs base their budgets on inaccurate estimates of revenue and expenditures and because other LEAs use their general fund to pay for overspending in other funds. In addition, some LEAs grant salary increases that are larger than the increases in the revenue used to pay for salaries. Finally, excessive administrative costs and declining attendance have contributed to the financial problems in some LEAs.

RECOMMENDATIONS

To ensure that LEAs are able to meet their financial obligations, they should take the following actions:

- Maintain a prudent fund balance; and
- Plan to spend less than they expect to receive if their fund balance is low.

To ensure that the LEAs provide the State Department of Education with accurate information for determining whether the LEAs have complied with their administrator limits as defined by the Education Code, Section 41402, the State Department of Education should take the following actions:

- Provide the LEAs with sufficiently detailed instructions so that employees may be correctly classified; and
- Provide the LEAs with consistent guidance as to which groups of employees should be reporting to the State Department of Education.

II

THE EARLY WARNING SYSTEM TO IDENTIFY SCHOOL DISTRICTS AND COUNTY OFFICES OF EDUCATION WITH FINANCIAL PROBLEMS NEEDS IMPROVEMENT

Recent legislation has established "early warning systems" to identify LEAs that may be unable to meet their financial obligations. The systems rely on reports that are prepared by the LEAs twice a year. The LEAs use these reports to assess their fiscal condition and recommend actions to correct the problems they identify. The early warning system for school districts and county offices of education (county offices) was implemented during 1986; for community college districts, a system will be implemented during 1987. While the early warning systems are too new for us to assess their effectiveness, we have determined that the system for school districts and county offices does not provide criteria or standard forms to use in assessing and reporting fiscal condition. In addition, current law does not give the county superintendents or the state agencies that review the reports the authority to ensure that local agencies comply with the reporting requirements of the early warning system or adopt and implement effective corrective action plans. Consequently, there is a lack of consistency in the way school districts and county offices assess and report their financial condition. In addition, the required reports were not always submitted, and many of the submitted reports were either incomplete or late. Unless school districts and county offices

prepare timely, accurate assessments of their financial condition and identify and correct their financial problems, they may require financial assistance from the State.

Until the early warning legislation was passed, the State relied primarily on the annual financial audits required by the Education Code to determine the financial condition of the LEAs. The department, the State Controller's Office, and the Board of Governors of the Community Colleges (board of governors) have used the information in the audit reports to prepare reports for the Legislature and to analyze the financial condition of the LEAs. While the annual audit reports have provided meaningful information about the financial condition of the LEAs, they do not necessarily provide timely information since the LEAs have not had to submit the audit reports until up to six months after the end of the fiscal year being audited.

The Early Warning System for School
Districts and County Offices of Education

Chapter 741, Statutes of 1985, which became effective on January 1, 1986, established an early warning system that would allow both local and state agencies to identify financially troubled school districts and county offices. At the state level, the department and the State Controller's Office jointly oversee the early warning system.

Chapter 741, Statutes of 1985, requires each school district and county office to submit to its governing board biannual reports

showing the financial and budgetary conditions of its district. Based upon the information in these reports, the governing board must certify in writing whether the district will be able to meet its financial obligations for the remainder of the year. There are three types of certifications: (1) a positive certification means that the school district or county office will be able to meet its obligations; (2) a qualified certification indicates that the school district or county office will or will not meet its current obligations if certain events occur; and (3) a negative certification means that the school district or county office will not be able to meet its obligations.

The school districts submit their certifications to the district governing board of education. If a district submits a negative or qualified certification, the governing board of education submits the district's report and certification to the department and the State Controller's Office. All county offices submit their own certifications to the county board of education, which then submits them to the department. In addition, county offices that have a negative or qualified certification must submit their reports and their certification to the state agencies.

A fiscal management advisory issued by the department notes that the department and the State Controller's Office will review and analyze the financial reports, the projections, and the transmittal form information of the school districts and county offices that submit negative and qualified certifications. Together, these agencies will

take appropriate action to determine whether plans have been adopted to correct the financial problems identified in the report. If the state agencies are satisfied that the school district or county office is appropriately addressing its problem, the state agencies take no further action. If the state agencies are not satisfied that the problem is being addressed, the state agencies contact the school district or county office directly. However, neither the county office nor the state agencies have the authority to compel the troubled school district or the county office to adopt and implement the corrective action plans. Furthermore, according to department officials, the department can assist the local agencies only if the local agencies request assistance.

In addition, according to Fiscal Management Advisory 86-02, issued by the department and the State Controller's Office, at a minimum, a district should examine cash and fund balance projections to determine whether it will be able to meet its financial obligations. Furthermore, the advisory states that districts that cannot make a positive certification must submit their financial projections, certifications, and a completed transmittal form to the State Controller's Office and to the department.

Lack of Consistency and Promptness
in Submitting Reports

During fiscal year 1985-86, only 48 of the 58 county offices submitted certifications to the department. Of these, 4 were qualified

and the remainder were positive. In addition, 28 school districts filed reports that indicated potential problems in satisfying their financial obligations. Of these, 27 filed qualified certifications, and one filed a negative certification. In the first reporting period of fiscal year 1986-87, only 20 of the 58 county offices submitted certifications to the department. Of these, 2 were qualified, and the remainder were positive. Additionally, one school district filed a negative certification, and 16 school districts filed qualified certifications. While all of the local agencies were able to meet their obligations during fiscal year 1985-86, the school district filing the negative certification in 1985-86 initiated legislation requesting an emergency loan during the 1986-87 fiscal year, and the school district filing the negative certification in fiscal year 1986-87 has requested assistance during the 1987-88 fiscal year. Both of these school districts had applied for the loan before filing their certifications.

We reviewed all 51 of the negative and qualified certifications submitted to the department. Most of the certifications were late and incomplete. In addition, the school districts and county offices submitted their financial information on a variety of forms, and they did not all base their qualified or negative certifications on the same criteria. Of the 40 certifications that were not submitted on time, 28 were up to one month late, 10 were up to two months late, and 2 were more than two months late. Of the 34 certifications that were incomplete, 20 did not include cash balance projections, and 10 did not

include fund balance projections. Seventeen of the certifications did not include a completed transmittal form, which is used to describe the district's or county office's financial problem and its corrective action plan. Initially, 38 of the certifications were incomplete when the department received them; however, the department obtained the missing information for 4 of these. According to the department, it did not obtain the missing information for the remaining 34 districts because the employee who reviews the certifications did not have time to do so.

We reviewed the certifications submitted by the 25 LEAs that we determined face financial difficulties to learn if they had submitted negative or qualified certifications. Our sample of 25 LEAs included 20 school districts and county offices. Of these, only 3 have submitted qualified certifications, one in fiscal year 1985-86 and 2 in fiscal year 1986-87. Furthermore, only one of the 3 school districts that ended fiscal year 1985-86 with a deficit in its general fund submitted a qualified certification. In addition, of the 6 school districts and one county office that we visited, 4 of the school districts submitted qualified certifications in fiscal year 1985-86. In fiscal year 1986-87, only one of the districts submitted a qualified certification. Three districts and the county office of education submitted positive certifications and two districts had not, as of February 27, 1987, submitted their certifications.

We cannot state whether there are school districts that should have submitted a qualified or negative certification but did not because there are no uniform standards to determine which school districts and county offices should submit qualified or negative certifications. Consequently, the assessments are not comparable, and the certifications may not be representative of the true financial condition of the school districts and county offices. For example, two school districts that submitted qualified certifications stated that they could not meet current obligations unless they could obtain a loan from the State or county. The county office of one of these school districts later changed the district's qualified certification to a negative certification. Another school district, which submitted a qualified certification, stated that it would be able to meet its current obligations provided that no "uninsured catastrophes" occurred.

On January 1, 1987, Chapter 1150, Statutes of 1986, became effective, changing the reporting periods and requiring the superintendent of any local agency that reports a negative cash balance or fund balance to provide a statement identifying the reasons for the negative balance and the steps to be taken to correct the negative balance by fiscal year's end. Furthermore, Chapter 1150, Statutes of 1986, states that, whenever a school district's governing board transmits a qualified or negative certification to the state agencies, the state agencies may direct the county superintendent of schools to conduct a comprehensive review of the financial and budgetary conditions of the district. If the school district submitted a

negative certification, the state agencies may conduct an on-site review, direct the county superintendent of schools to conduct a review of the district, or direct the district to prepare alternative plans for resolving the identified fiscal problem.

Because Chapter 1150, Statutes of 1986, did not become effective until January 1, 1987, and the first certifications to be filed under this law will not be received until March 31, 1987, it is too early to determine its effect on the early warning system. However, while this legislation makes some improvements in the early warning system, it does not establish criteria for the school districts and county offices to use to assess their financial condition, and it does not establish standard report forms. In addition, it does not provide the county offices or the state agencies with the authority to ensure that local agencies comply with the reporting requirements of the early warning system or adopt and implement effective corrective action plans.

In addition to implementing the early warning system, the department has established the Financial Management Advisory Committee (FMAC), which is working on a pilot project to improve the financial management of school districts and county offices. The FMAC, which is composed of personnel from the department and other state and local agencies, is focusing its efforts on four projects: a new program cost accounting system, a revised budgeting process, a new interim reporting system, and a restructured set of school district financial statements.

The FMAC's reporting, accounting, and budget systems are expected to provide better information on local agency operations. In fiscal year 1986-87, 226 local agencies are voluntarily participating in the FMAC pilot project. According to department officials, they plan to implement the FMAC's reporting, accounting, and budget systems in all local agencies in fiscal year 1988-89.

The Early Warning System To
Identify Community College
Districts With Financial Problems

In 1986, the Legislature adopted Chapter 1486, Statutes of 1986. The intent of this legislation, which became effective on January 1, 1987, was to develop an early warning system to identify community college districts in questionable fiscal condition. In addition, Chapter 1486, Statutes of 1986, increased the authority of the Chancellor of the California Community Colleges (chancellor) over districts that are experiencing financial difficulties.

Chapter 1486, Statutes of 1986, requires each district to submit to its governing board a quarterly report based on the measurements and standards established by the board. When the local governing board has certified the report, the district submits a certified copy of the report to the county superintendent and the chancellor. The county superintendent is required to review the certified report. If the county superintendent determines that the district is in a questionable fiscal position based on the criteria

developed by the board of governors or that the district has not complied with the reporting requirements, the county superintendent must report this to the chancellor with copies of the related certified reports.

If the chancellor determines that the district is in a questionable fiscal condition, the chancellor will require the district, the county superintendent, or both, to report the actions they plan to take to correct the problems. If the chancellor determines that the proposed actions are inadequate, Chapter 1486, Statutes of 1986, authorizes the chancellor to direct the district to prepare and adopt a detailed plan for achieving financial stability and an educational plan demonstrating the impact of the fiscal plan on the educational program. In addition, the chancellor may take a number of actions if he determines that the plan is inadequate. These actions include conducting a management review or audit of the district or monitoring the implementation of the corrective action plan. If the corrective action plan fails to achieve financial stability, Chapter 1486, Statutes of 1986, requires the chancellor to take several actions. For example, the chancellor may require that all subsequent actions of the district to implement the fiscal and educational plans be submitted for prior approval. The chancellor may also reduce or withhold any apportionment to the district. The chancellor is required to report to the board of governors, the Legislature, the director of finance, and the governor any action taken against the district and any action taken by the district.

Because Chapter 1486, Statutes of 1986, did not become effective until January 1, 1987, it is too early to determine whether the early warning system will be effective. In addition, we were unable to test the standards and measures that the board of governors is required to develop to assess the financial condition of districts because, as of February 17, 1987, the board had not adopted the standards and measures. The board of governors is currently awaiting responses from the districts regarding the standards and measures it has drafted.

CONCLUSION

Because the early warning systems to identify local education agencies with financial problems are so new, we cannot assess the effectiveness of these systems. However, there are weaknesses in the early warning system for school districts and county offices of education that may impede its effectiveness. The system does not provide criteria or standard report forms for local agencies to use to assess their financial condition. In addition, current law does not give the county superintendents, the State Department of Education, or the State Controller's Office the authority to ensure that local agencies comply with the reporting requirements of the early warning system or adopt and implement effective corrective action plans. As a result, there is a lack of consistency in the way school districts and

county offices assess and report their financial condition. In addition, some school districts and county offices either do not submit required reports, submit reports that are late, or submit reports that are incomplete. Unless school districts and county offices prepare timely, accurate assessments of their financial condition to identify and correct financial problems, they may require financial assistance from the State.

RECOMMENDATIONS

To improve the early warning system and ensure that school districts and county offices of education comply with all requirements of the early warning system, the Legislature and the governor should take the following actions:

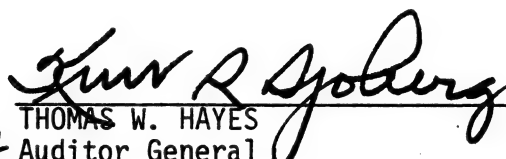
- Adopt legislation requiring the State Department of Education, in conjunction with the State Controller's Office and county offices of education, to develop criteria by which the school districts and county offices of education are to assess their fiscal condition. In addition, require the department to develop standard report forms to be used by the school districts and county offices of education; and

- Adopt legislation that gives the State Department of Education and the State Controller's Office the authority to enforce the requirements of the early warning system similar to the authority granted to the Chancellor of the California Community Colleges by the Education Code, Sections 84044 and 84045.

To ensure that the early warning system for community college districts is effective, the Board Of Governors of the California Community Colleges should closely monitor the early warning system to ensure that it achieves the desired results.

We conducted this review under the authority vested in the Auditor General by Section 10500 et seq. of the California Government Code and according to generally accepted governmental auditing standards. We limited our review to those areas specified in the audit scope section of this report.

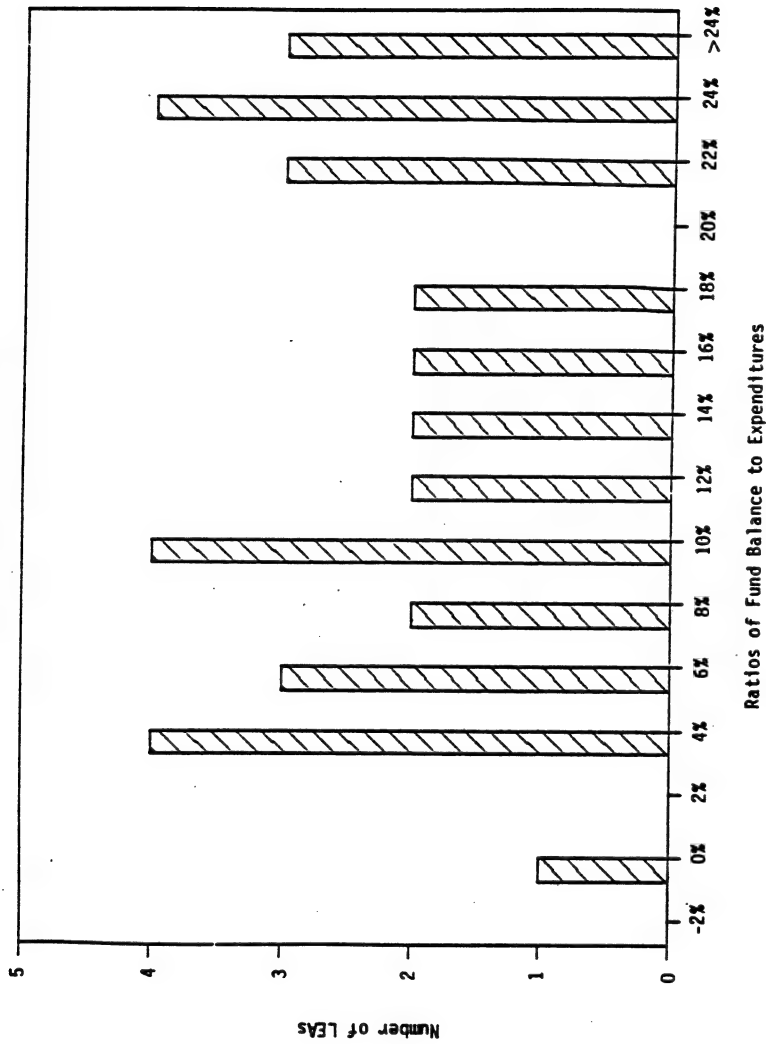
Respectfully submitted,


for THOMAS W. HAYES
Auditor General

Date: March 23, 1987

Staff: Sally Filliman, CPA, Audit Manager
Philip Jelichich, CPA, Audit Manager
Sylvia Hensley, CPA
Karen McKenna, CPA
Jeff Winston, CPA
Cornelius Paul Frydendal, CPA
Mark Lamb, CPA
Jim Rostron, CPA
Denise L. Vose, CPA

DISTRIBUTION OF RATIOS OF FUND BALANCE TO EXPENDITURES
FOR 32 SMALL LOCAL EDUCATIONAL AGENCIES
AS OF JUNE 30, 1986



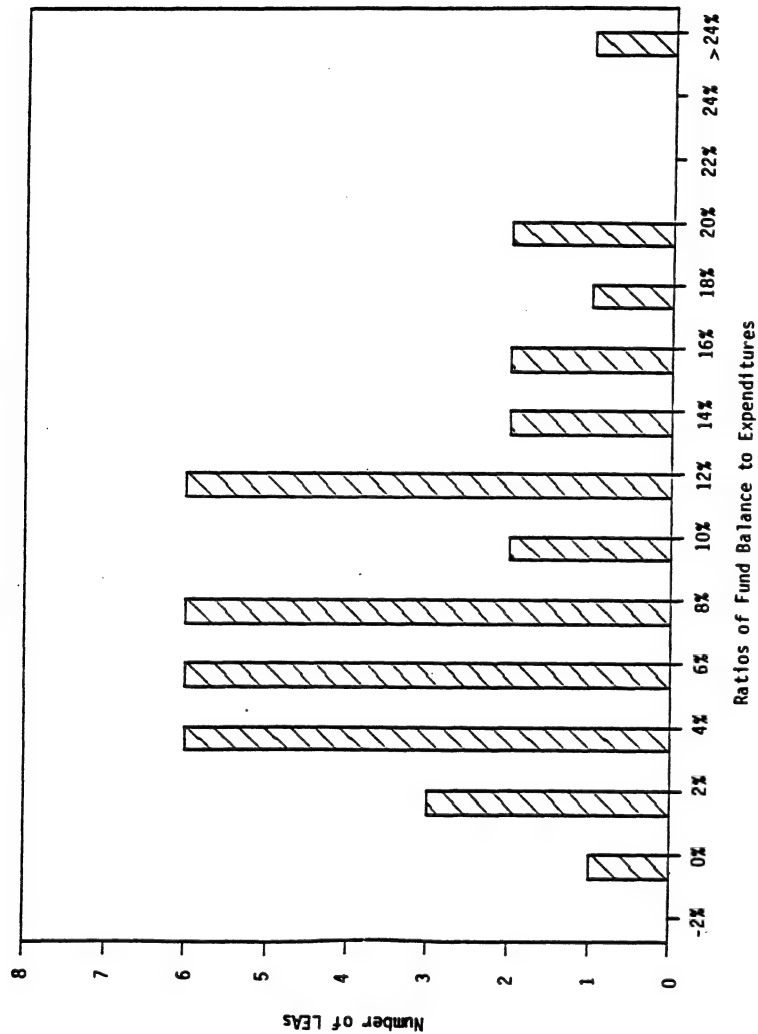
Local Educational Agency	Expenditures 1985-86	Fund Balance 6/30/86	Ratio 6/30/86
FRIANT UNION*	306,977	(660)	-0.21%
WINDSOR UNION*	3,013,180	67,652	2.25%
UNION HILL *	807,982	24,547	3.04%
GUERNEVILLE ELEMENTARY*	1,759,871	64,343	3.66%
Julian Union High*	1,076,830	42,540	3.95%
Fruitvale Elementary*	3,053,017	128,878	4.22%
Hughes-Elizabeth Lakes Union Elementary*	1,039,701	56,852	5.47%
Mark West Union Elementary*	1,462,316	82,950	5.67%
Spreckles Union Elementary	1,580,435	115,564	7.31%

Sundale Union Elementary	1,051,712	80,251	7.63%
Napa County Office of Education	7,186,052	602,902	8.39%
Bend Elementary	254,562	21,728	8.54%
Gridley Union High	1,821,980	167,120	9.17%
Citrus Community College	16,558,239	1,558,392	9.41%
Guadalupe Union Elementary	2,118,825	242,734	11.46%
Etiwanda Elementary	2,413,334	283,400	11.74%
Reed Union Elementary	3,363,605	403,840	12.01%
Round Valley Unified	2,155,630	270,205	12.53%
Durham Unified	2,843,543	401,619	14.12%
Salida Union Elementary	2,193,345	341,764	15.58%
Bolinas-Stinson Union Elementary	844,567	136,897	16.21%
Newcastle Elementary	781,500	127,308	16.29%
Kit Carson Union Elementary	1,118,398	228,714	20.45%
Island Union Elementary	609,690	126,263	20.71%
Indian Springs Elementary	587,966	127,693	21.72%
Round Valley Joint Elementary	429,522	99,143	23.08%
Tulelake Basin Joint Unified	2,095,794	486,344	23.21%
Montecito Union Elementary	1,124,478	263,088	23.40%
Stoney Creek Joint Unified	1,075,584	256,637	23.86%
Jefferson Elementary	66,758	62,517	93.65%
Vista Del Mar Union Elementary	445,405	596,257	133.87%
Bradley Union Elementary	155,413	324,069	208.52%
Weighted Average	2,043,632	243,486	11.92%

*This LEA has a low fund balance.

NOTE: District names in UPPER CASE were part of the sample of 25 LEAs that we determined face potential financial problems.

**DISTRIBUTION OF RATIOS OF FUND BALANCE TO EXPENDITURES
FOR 38 MEDIUM LOCAL EDUCATIONAL AGENCIES
AS OF JUNE 30, 1986**



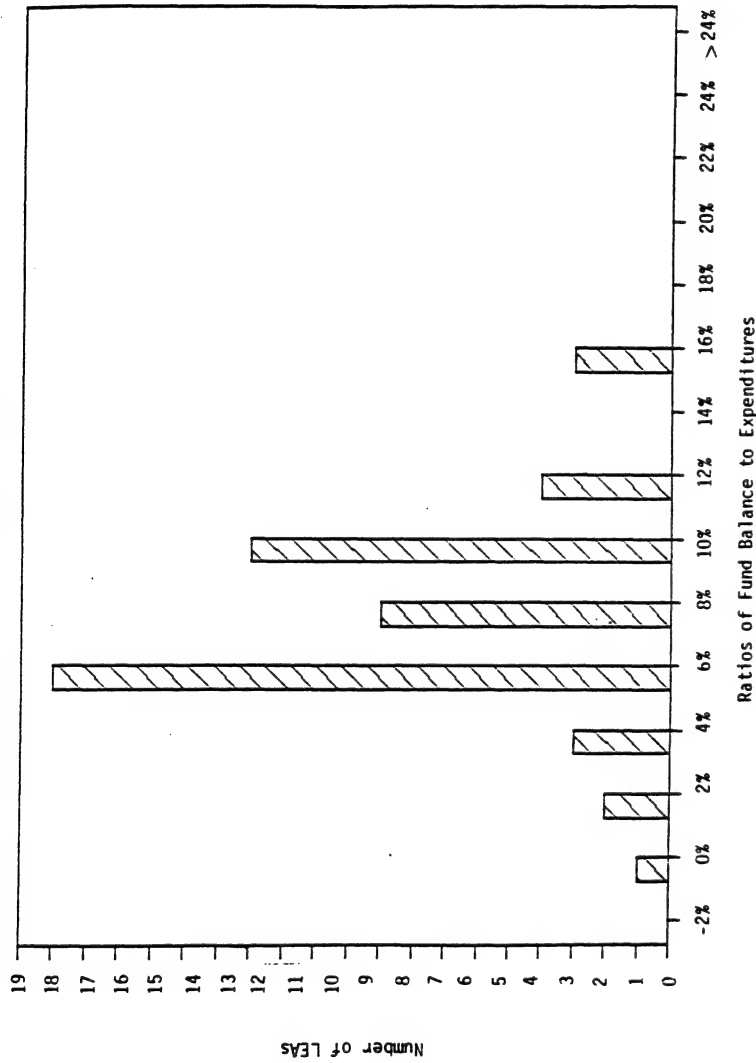
Local Educational Agency	Expenditures 1985-86	Fund Balance 6/30/86	Ratio 6/30/86
SANTA ROSA ELEMENTARY*	11,485,599	(65,254)	-0.57%
SAN MATEO COUNTY SUPERINTENDENT OF SCHOOLS*	33,121,639	157,049	0.47%
RIM OF THE WORLD UNIFIED*	14,958,521	131,027	0.88%
ALBANY UNIFIED*	8,098,679	160,333	1.98%
WILLIAM S. HART UNION HIGH*	33,241,163	830,955	2.50%
AMADOR VALLEY JOINT UNION HIGH*	15,567,413	508,770	3.27%
Mill Valley Elementary*	5,344,183	178,451	3.34%
BEAUMONT UNIFIED*	8,048,439	272,741	3.39%
Silver Valley Unified*	7,050,724	258,334	3.66%

El Segundo Unified*	7,232,750	271,696	3.76%
Cambrian Elementary	6,948,062	282,205	4.06%
Lemoore Union High	4,946,429	224,424	4.54%
ARCADIA UNIFIED	22,530,660	1,166,416	5.18%
Milpitas Unified	27,584,167	1,556,573	5.64%
SANTA MONICA COMMUNITY COLLEGE	32,248,948	1,878,375	5.82%
CONTRA COSTA COMMUNITY COLLEGE	55,475,806	3,323,574	5.99%
Woodland Joint Unified	20,875,465	1,290,899	6.18%
Mother Lode Union Elementary	3,825,680	252,980	6.61%
Pleasant Valley Elementary (Camarillo)	15,220,793	1,106,907	7.27%
Los Banos Unified	9,630,264	705,311	7.32%
Centralia Elementary	14,163,059	1,071,970	7.57%
Central Unified	11,480,277	885,945	7.72%
Baldwin Park Unified	42,170,926	3,374,218	8.00%
Gridley Union Elementary	3,293,962	320,764	9.74%
Chowchilla Elementary	3,413,947	341,446	10.00%
Cucamonga Elementary	4,207,994	428,738	10.19%
Goleta Union Elementary	16,136,222	1,662,207	10.30%
South Whittier Elementary	10,474,539	1,113,016	10.63%
Lennox Elementary	13,779,615	1,472,453	10.69%
Sylvan Union Elementary	12,598,941	1,440,060	11.43%
Pasadena Community College	39,860,098	5,509,129	13.82%
Carpinteria Unified	6,857,175	953,754	13.91%
Sonoma County Office	16,459,695	2,589,826	15.73%
Lincoln Unified	22,467,039	3,549,486	15.80%
Livermore Valley Joint Unified	31,302,697	5,267,863	16.83%
Dixie Elementary	5,547,022	1,046,354	18.86%
Sunnyvale Elementary	18,944,827	3,765,129	19.87%
Walnut Creek Elementary	7,429,432	2,632,644	35.44%
Weighted Averages	16,421,654	1,366,231	8.32%

*This LEA has a low fund balance.

NOTE: District names in UPPER CASE were part of the sample of 25 LEAs that we determined face potential financial problems.

**DISTRIBUTION OF RATIOS OF FUND BALANCE TO EXPENDITURES
FOR 54 LARGE LOCAL EDUCATIONAL AGENCIES
AS OF JUNE 30, 1986**



Local Educational Agency	Expenditures 1985-86	Fund Balance 6/30/86	Ratio 6/30/86
NEWPORT-MESA UNIFIED*	71,710,027	(833,509)	-1.16%
COAST COMMUNITY COLLEGE*	89,020,367	164,868	0.19%
SACRAMENTO CITY UNIFIED*	144,520,184	2,546,210	1.76%
Pasadena Unified*	75,421,708	1,585,726	2.10%
Los Angeles County Office of Education*	196,711,434	4,702,562	2.39%
SAN FRANCISCO UNIFIED*	195,721,177	5,548,309	2.83%
SAN DIEGO COMMUNITY COLLEGE*	71,940,000	3,483,000	4.84%
RIVERSIDE UNIFIED	76,100,400	3,096,607	4.07%
HAYWARD UNIFIED	54,350,184	2,217,924	4.08%
LOS ANGELES COMMUNITY COLLEGE	193,832,900	7,778,583	4.01%
San Juan Unified	140,332,641	6,562,335	4.68%
Huntington Beach Union High	71,915,808	3,380,018	4.70%
Simi Valley Unified	56,323,865	2,778,674	4.93%
Compton Unified	94,005,045	4,704,513	5.00%
Santa Ana Unified	108,878,590	5,467,964	5.02%
Grossmont Union High	71,866,673	3,613,647	5.03%

CONEJO VALLEY UNIFIED	54,441,219	2,793,886	5.13%
San Diego Unified	411,102,167	21,799,594	5.30%
Hacienda-LaPuente Unified	68,891,440	3,739,993	5.43%
FONTANA UNIFIED	46,855,367	2,561,059	5.47%
ABC UNIFIED	74,239,099	4,074,686	5.49%
Visalia Unified	54,124,491	3,080,808	5.69%
Elk Grove Unified	52,015,938	2,965,760	5.70%
Mt. Diablo Unified	91,952,120	5,254,065	5.71%
San Jose City Unified	103,736,223	6,216,646	5.99%
East Side Union High	84,915,888	5,100,957	6.01%
Poway City Unified	52,100,059	3,173,111	6.09%
San Diego County Office of Education	47,568,065	2,947,422	6.20%
Torrance Unified	61,362,083	3,961,916	6.46%
Garden Grove Unified	117,895,072	7,789,217	6.61%
Placentia Unified	55,179,268	3,659,182	6.63%
Orange Unified	79,191,401	5,319,196	6.72%
Inglewood Unified	46,436,870	3,383,468	7.29%
Lodi Unified	56,902,907	4,193,582	7.37%
Fremont Unified	76,907,959	6,157,396	8.01%
Montebello Unified	93,741,710	7,530,654	8.03%
Irvine Unified	60,061,735	4,933,524	8.21%
Rowland Unified	51,790,168	4,290,805	8.28%
Kern Union High	71,113,859	5,914,225	8.32%
Los Angeles Unified	2,051,333,000	174,830,000	8.52%
Fairfield-Sutsum Unified	44,155,542	3,781,804	8.56%
Anaheim Union High	88,106,123	7,806,101	8.86%
Corona-Norco Unified	50,296,699	4,637,569	9.22%
Pomona Unified	71,558,883	6,761,989	9.45%
Ontario-Montclair Elementary	50,461,430	4,824,192	9.56%
Saddleback Valley Unified	71,533,355	7,096,906	9.93%
San Bernardino City Unified	106,918,909	10,630,628	9.94%
Glendale Unified	61,249,977	6,224,905	10.16%
Bakersfield City Elementary	57,434,649	6,072,950	10.57%
Chino Unified	49,172,474	5,284,196	10.75%
Long Beach Unified	196,201,978	22,105,188	11.27%
Riverside County Superintendent of Schools	39,035,067	5,504,568	14.10%
Norwalk-LaMirada Unified	59,527,114	9,068,423	15.23%
Capistrano Unified	56,767,904	8,864,861	15.62%
Weighted Averages	123,682,303	8,539,497	6.90%

*This LEA has a low fund balance.

NOTE: District names in UPPER CASE were part of the sample of 25 LEAs that were determined

APPENDIX B

JUNE 30, 1986, FUND BALANCE AND FISCAL YEAR 1985-86 REVENUES AND EXPENDITURES FOR 124 LOCAL EDUCATIONAL AGENCIES

Local Educational Agency	LEA's Ending Fund Balance at June 30, 1986	Fiscal Year 1985-86 Revenues	Fiscal Year 1985-86 Expenditures	Difference Between Expenditures and Revenues
ABC UNIFIED	\$ 4,074,686	\$ 74,417,242	\$ 74,239,099	\$ 178,143
ALBANY UNIFIED	160,333	8,186,207	8,098,679	87,528
AMADOR VALLEY JOINT UNION HIGH	508,770	15,318,791	15,567,413	(248,622)*
Ahaheim Union High	7,806,101	88,977,693	88,106,123	871,570
ARCADIA UNIFIED	1,166,416	23,222,624	22,530,660	691,964
Bakersfield City Elementary	6,072,950	60,583,999	57,434,649	3,149,350
Baldwin Park Unified	3,374,218	44,208,614	42,170,926	2,037,688
BEAUMONT UNIFIED	272,741	8,057,004	8,048,439	8,565
Bend Elementary	21,728	252,196	254,562	(2,366)*
Bolinas-Stinson Union Elementary	136,897	862,641	844,567	18,074
Bradley Union Elementary	324,069	179,286	155,413	23,873
Cambrian Elementary	282,205	6,818,469	6,948,062	(129,593)*
Capistrano Unified	8,864,861	60,171,237	56,767,904	3,403,333
Carpenteria Unified	953,754	7,077,136	6,857,175	219,961
Central Unified	885,945	11,655,340	11,480,277	175,063
Centralia Elementary	1,071,970	14,377,140	14,163,059	214,081
Chino Unified	5,284,196	51,067,605	49,172,474	1,895,131
Chowchilla Elementary	341,446	3,642,053	3,413,947	228,106
Citrus Community College	1,558,392	16,836,429	16,558,239	278,190
COAST COMMUNITY COLLEGE	164,868	86,375,499	89,020,367	(2,644,868)*
Compton Unified	4,704,513	97,662,344	94,005,045	3,657,299
CONEJO VALLEY UNIFIED	2,793,886	56,327,115	54,441,219	1,885,896
CONTRA COSTA COMMUNITY COLLEGE	3,323,574	55,322,656	55,475,806	(153,150)*
Corona-Norco Unified	4,637,569	52,088,443	50,296,699	1,791,744
Cucamonga Elementary	428,738	4,439,098	4,207,994	231,104
Dixie Elementary	1,046,354	5,531,356	5,547,022	(15,666)*
Durham Unified	401,619	2,906,409	2,843,543	62,866
East Side Union High	5,100,957	87,392,358	84,915,888	2,476,470
El Segundo Unified	271,696	7,293,599	7,232,750	60,849
Elk Grove Unified	2,965,760	53,634,669	52,015,938	1,618,731
Etiwanda Elementary	283,400	2,447,486	2,413,334	34,152
Fairfield-Suisun Unified	3,781,804	46,142,686	44,155,542	1,987,144
FONTANA UNIFIED	2,561,059	47,944,676	46,855,367	1,089,309
Fremont Unified	6,157,396	80,734,007	76,907,959	3,826,048
FRIANT UNION	(660)	280,204	306,977	(26,773)*
Fruitvale Elementary	128,878	3,109,235	3,053,017	56,218
Garden Grove Unified	7,789,217	121,162,413	117,895,072	3,267,341
Glendale Unified	6,224,905	64,050,116	61,249,977	2,800,139
Goleta Union Elementary	1,662,207	16,133,070	16,136,222	(3,152)*
Gridley Union Elementary	320,764	3,468,730	3,293,962	174,768
Gridley Union High	167,120	1,824,565	1,821,980	2,585
Grossmont Union High	3,613,647	73,925,127	71,866,673	2,058,454
Guadalupe Union Elementary	242,734	2,186,243	2,118,825	67,418
GUERNEVILLE ELEMENTARY	64,343	1,784,637	1,759,871	24,766
Hacienda-LaPuente Unified	3,739,993	71,425,277	68,891,440	2,533,837
HAYWARD UNIFIED	2,217,924	55,474,009	54,350,184	1,123,825
Hughes-Elizabeth Lakes Union Elementary	56,852	1,019,568	1,039,701	(20,133)*
Huntington Beach Union High	3,380,018	73,935,602	71,915,808	2,019,794
Indian Springs Elementary	127,693	632,792	587,966	44,826
Inglewood Unified	3,383,468	48,149,171	46,436,870	1,712,301
Irvine Unified	4,933,524	63,138,226	60,061,735	3,076,491
Island Union Elementary	126,263	634,088	609,690	24,398
Jefferson Elementary (San Benito)	62,517	76,828	66,758	10,070
Julian Union High	42,540	1,057,593	1,076,830	(19,237)*
Kern Union High	5,914,225	72,624,900	71,113,859	1,511,041
Kit Carson Union Elementary	228,714	1,035,506	1,118,398	(82,892)*
Lemoore Union High	224,424	4,926,802	4,946,429	(19,627)*
Lennox Elementary	1,472,453	14,361,803	13,779,615	582,188
Lincoln Unified	3,549,486	23,327,485	22,467,039	860,446
Livermore Valley Joint Unified	5,267,863	32,796,875	31,302,697	1,494,178

*This LEA's expenditures exceeded revenues for fiscal year 1985-86.

NOTE: District names in UPPER CASE were part of our sample of 25 LEAs that we determined face potential financial problems.

Local Educational Agency	LEA's Ending Fund Balance at June 30, 1986	Fiscal Year 1985-86 Revenues	Fiscal Year 1985-86 Expenditures	Difference Between Expenditures and Revenues
Lodi Unified	4,193,582	58,152,368	56,902,907	1,249,461
Long Beach Unified	22,105,188	209,577,604	196,201,978	13,375,626
LOS ANGELES COMMUNITY COLLEGE	7,778,583	206,665,165	193,832,900	12,832,265
Los Angeles County Office of Education	4,702,562	201,075,350	196,711,434	4,363,916
Los Angeles Unified	174,830,000	2,101,205,000	2,051,333,000	49,872,000
Los Banos Unified	705,311	9,617,956	9,630,264	(12,308)*
Mark West Union Elementary	82,950	1,436,939	1,462,316	(25,377)*
Mill Valley Elementary	178,451	5,215,322	5,344,183	(128,861)*
Milpitas Unified	1,556,573	27,391,143	27,584,167	(193,024)*
Montebello Unified	7,530,654	96,153,851	93,741,710	2,412,141
Montecito Union Elementary	263,088	1,156,271	1,124,478	31,793
Mother Lode Union Elementary	252,980	3,955,576	3,825,680	129,896
Mt. Diablo Unified	5,254,065	95,766,541	91,952,120	3,814,421
Napa County Office of Education	602,902	7,126,025	7,186,052	(60,027)*
Newcastle Elementary	127,308	815,266	781,500	33,766
NEWPORT-MESA UNIFIED	(833,509)	69,507,431	71,710,027	(2,202,596)*
Norwalk-LaMirada Unified	9,068,423	60,503,424	59,527,114	976,310
Ontario-Montclair Elementary	4,824,192	52,138,815	50,461,430	1,677,385
Orange Unified	5,319,196	81,608,022	79,191,401	2,416,621
Pasadena Area Community College	5,509,129	42,121,066	39,860,098	2,260,968
Pasadena Unified	1,585,726	73,414,989	75,421,708	(2,006,719)*
Placentia Unified	3,659,182	55,388,859	55,179,268	209,591
Pleasant Valley Elementary (Camarillo)	1,106,907	15,922,135	15,220,793	701,342
Pomona Unified	6,761,989	74,240,903	71,533,355	2,707,548
Poway Unified	3,173,111	53,202,706	52,100,059	1,102,647
Reed Union Elementary	403,840	3,447,086	3,363,605	83,481
RIM OF THE WORLD UNIFIED	131,027	14,788,185	14,958,521	(170,336)*
Riverside County Superintendent of Schools	5,504,568	40,190,747	39,035,067	1,155,680
RIVERSIDE UNIFIED	3,096,607	78,674,697	76,100,400	2,574,297
Round Valley Joint Elementary	99,143	474,674	429,522	45,152
Round Valley Unified	270,205	2,288,122	2,155,630	132,492
Rowland Unified	4,290,805	54,940,627	51,790,168	3,150,459
SACRAMENTO CITY UNIFIED	2,546,210	143,829,549	144,520,184	(690,635)*
Saddleback Valley Unified	7,096,906	72,358,656	71,474,037	884,619
Salida Union	341,764	2,193,331	2,193,345	(53,014)*
San Bernardino City Unified	10,630,628	111,642,444	106,918,909	4,723,535
SAN DIEGO COMMUNITY COLLEGE	3,483,000	74,309,000	71,940,000	2,369,000
San Diego County Office of Education	2,974,422	48,810,730	47,568,065	1,242,665
San Diego Unified	21,799,594	422,342,830	411,102,167	11,240,663
SAN FRANCISCO UNIFIED	5,548,309	201,579,567	195,721,177	5,858,390
San Jose City Unified	6,216,646	106,567,606	103,736,223	2,831,383
San Juan Unified	6,562,335	144,056,459	140,332,641	3,723,818
SAN MATEO COUNTY SUPERINTENDENT OF SCHOOLS	157,049	34,273,309	33,121,639	1,151,670
Santa Ana Unified	5,467,964	112,048,357	108,878,590	3,169,767
SANTA MONICA COMMUNITY COLLEGE	1,878,375	33,397,443	32,248,948	1,148,495
SANTA ROSA ELEMENTARY	65,254)	11,712,248	11,485,599	226,649
Silver Valley Unified	258,334	7,180,617	7,050,724	129,893
Simi Valley Unified	2,778,674	55,210,354	56,323,865	(1,113,511)*
Sonoma County Office of Education	2,589,826	17,019,983	16,459,695	560,288
South Whittier Elementary	1,113,016	11,125,865	10,474,539	651,326
Spreckles Union Elementary	115,564	1,690,186	1,580,435	109,751
Stony Creek Joint Unified	256,637	1,050,229	1,075,584	(25,355)*
Sundale Union Elementary	80,251	1,067,690	1,051,712	15,978
Sunnyvale Elementary	3,765,129	19,327,686	18,944,827	382,859
Sylvan Union Elementary	1,440,060	13,076,744	12,598,941	477,803
Torrance Unified	3,961,916	62,919,144	61,362,083	1,557,061
Tulelake Basin Joint Unified	486,344	2,097,965	2,095,794	2,171
UNION HILL	24,547	820,239	807,982	12,257
Visalia Unified	3,080,808	55,780,544	54,124,491	1,656,053
Vista Del Mar Union Elementary	596,257	613,904	445,405	168,499
Walnut Creek Elementary	2,632,644	7,483,924	7,429,432	54,492
WILLIAM S. HART UNION HIGH	830,955	34,103,270	33,241,163	862,107
WINDSOR UNION	67,652	3,082,319	3,013,180	69,139
Woodland Joint Unified	1,290,899	20,759,449	20,875,465	(116,016)*

*This LEA's expenditures exceeded revenues for fiscal year 1985-86.

NOTE: District names in UPPER CASE were part of our sample of 25 LEAs that we determined face potential financial problems.

APPENDIX C

AVERAGE DAILY ATTENDANCE 124 LOCAL EDUCATIONAL AGENCIES FISCAL YEARS 1981-82 THROUGH 1985-86

Local Educational Agency	Fiscal Year 1981-82	Fiscal Year 1982-83	Fiscal Year 1983-84	Fiscal Year 1984-85	Fiscal Year 1985-86	Net Change	Percentage
<u>County Offices of Education</u>							
LOS ANGELES	16,231	14,692	16,444	17,341	19,386	3,155	19.44
Napa	903	832	910	823	884	(19)	-2.10
Riverside	4,746	4,746	4,925	4,940	5,406	660	13.91
San Diego	5,743	6,834	7,413	7,348	7,785	2,042	35.56
SAN MATEO	1,697	1,634	2,047	1,904	2,069	372	21.92
Sonoma	1,349	1,312	1,459	1,476	1,590	241	17.87
Subtotals	30,669	30,050	33,198	33,832	37,120	6,451	21.03
<u>Community College Districts</u>							
Citrus	6,199	6,024	5,784	5,182	5,503	(696)	-11.23
SANTA MONICA	11,747	11,546	11,172	10,658	10,765	(982)	-8.36
CONTRA COSTA	19,899	19,475	17,164	18,415	18,284	(1,615)	-8.12
Pasadena Area	16,243	14,752	14,671	13,511	13,917	(2,326)	-14.32
COAST	35,566	32,273	29,641	26,923	26,323	(9,243)	-25.99
SAN DIEGO	38,521	35,192	31,469	31,535	31,039	(7,482)	-19.42
Los Angeles	73,679	62,391	62,554	53,813	49,330	(24,349)	-33.05
Subtotals	201,854	191,653	172,455	160,037	155,161	(46,693)	-23.13
<u>Small School Districts</u>							
Bend Elementary	63	57	63	60	65	2	3.17
Bolinas-Stinson Union Elementary	220	209	206	198	210	(10)	-4.55
Bradley Union Elementary	31	34	31	32	22	(9)	-29.03
Durham Unified	800	806	810	838	849	49	6.13
Etiwanda Elementary	597	626	635	715	833	236	39.53
FRIANT UNION	59	64	70	74	72	13	22.03
Fruitvale Elementary	563	573	612	664	719	156	27.71
Gridley Union High	576	552	549	526	533	(43)	-7.47
Guadalupe Union Elementary	678	644	605	621	692	14	2.06
GUERNEVILLE ELEMENTARY	540	479	545	525	521	(19)	-3.52
Hughes-Elizabeth Lakes Union Elem.	218	236	230	260	281	63	28.90
Indian Springs Elementary	37	36	41	52	52	15	40.54
Island Union Elementary	185	206	211	196	205	20	10.81
Jefferson Elementary (San Benito)	8	11	11	9	9	1	12.50
Julian Union High	196	195	200	200	198	2	1.02
Kit Carson Union Elementary	327	318	332	346	350	23	7.03
Mark West Union Elementary	453	433	458	454	462	9	1.99
Montecito Union Elementary	286	264	280	286	289	3	1.05
Newcastle Elementary	272	255	253	237	256	(16)	-5.88
Reed Union Elementary	938	851	772	777	787	(151)	-16.10
Round Valley Joint Elementary	162	169	162	160	134	(28)	-17.28
Round Valley Unified	430	411	407	376	395	(35)	-8.14
Salida Union Elementary	527	540	546	623	769	242	45.92
Spreckles Union Elementary	521	531	506	498	454	(67)	-12.86
Stony Creek Joint Unified	149	136	132	127	136	(13)	-8.72
Sundale Union Elementary	395	396	380	363	369	(26)	-6.58
Tulelake Basin Joint Unified	454	444	455	452	482	28	6.17
UNION HILL	238	239	245	275	300	62	26.05
Vista Del Mar Union Elementary	64	78	74	71	56	(8)	-12.50
WINDSOR UNION	725	877	891	915	963	238	32.83
Subtotals	10,712	10,670	10,712	10,930	11,463	751	7.01

NOTE: District names in UPPER CASE were part of our sample of 25 LEAs that we determined face potential financial problems.

Local Educational Agency	Fiscal Year 1981-82	Fiscal Year 1982-83	Fiscal Year 1983-84	Fiscal Year 1984-85	Fiscal Year 1985-86	Net Change	Percentage
<u>Medium School Districts</u>							
ALBANY UNIFIED	2,303	2,404	2,411	2,435	2,572	269	11.68
AMADOR VALLEY JOINT UNION HIGH	4,893	4,939	4,915	5,066	5,198	305	6.23
ARCADIA UNIFIED	8,022	7,740	7,573	7,452	7,420	(602)	-7.50
Baldwin Park Unified	15,069	15,529	16,039	16,453	17,027	1,958	12.99
BEAUMONT UNIFIED	2,530	2,593	2,568	2,571	2,627	97	3.83
Cambrian Elementary	2,176	2,210	2,086	2,013	2,031	(145)	-6.66
Carpinteria Unified	2,237	2,288	2,325	2,294	2,377	140	6.26
Central Unified		2,980*	3,106	3,155	3,359	379	12.72
Centralia Elementary	4,016	3,848	3,744	3,853	3,961	(55)	-1.37
Chowchilla Elementary	1,075	1,099	1,154	1,178	1,174	99	9.21
Cucamonga Elementary	1,211	1,263	1,320	1,350	1,452	241	19.90
Dixie Elementary	1,627	1,460	1,295	1,165	1,093	(534)	-32.82
El Segundo Unified	2,021	1,893	1,908	1,932	1,973	(48)	-2.38
Goleta Union Elementary	3,760	3,566	3,447	3,399	3,417	(343)	-9.12
Gridley Union Elementary	1,122	1,127	1,155	1,157	1,205	83	7.40
Lemoore Union High	1,230	1,264	1,232	1,289	1,289	59	4.80
Lennox Elementary	4,620	4,622	4,754	4,770	4,745	125	2.71
Lincoln Unified	6,775	6,990	7,039	7,231	7,777	1,002	14.79
Livermore Valley Joint Unified	11,371	11,104	10,789	10,549	10,569	(802)	-7.05
Los Banos Unified	2,694	2,798	2,819	2,955	3,083	389	14.44
Mill Valley Elementary	1,844	1,789	1,692	1,641	1,613	(231)	-12.53
Milpitas Unified	8,218	8,136	7,729	7,892	8,187	(31)	-0.38
Mother Lode Union Elementary	1,179	1,171	1,170	1,158	1,310	131	11.11
Pleasant Valley Elementary (Camarillo)	5,559	5,437	5,394	5,358	5,491	(68)	-1.22
RIM OF THE WORLD UNIFIED	4,288	4,274	4,384	4,419	4,531	243	5.67
SANTA ROSA ELEMENTARY	3,423	3,484	3,510	3,683	3,916	493	14.40
Silver Valley Unified	1,279	1,426	1,624	1,702	1,800	521	40.73
South Whittier Elementary	3,251	3,261	3,315	3,253	3,337	86	2.65
Sunnyvale Elementary	5,418	5,349	5,187	5,210	5,008	(410)	-7.57
Sylvan Union Elementary	4,214	4,185	4,185	4,334	4,638	424	10.06
Walnut Creek Elementary	2,353	2,334	2,233	2,236	2,309	(44)	-1.87
WILLIAM S. HART UNION HIGH	8,857	9,368	9,407	9,194	9,844	987	11.14
Woodland Joint Unified	6,727	6,743	6,682	6,751	6,980	253	3.76
Subtotals	135,362	138,674	138,191	139,098	143,313	7,951	5.87
<u>Large School Districts</u>							
ABC UNIFIED	25,307	25,144	24,730	24,607	25,210	(97)	-0.38
Anaheim Union High	25,866	25,645	25,423	24,362	21,414	(4,452)	-17.21
Bakersfield City Elementary	17,144	17,656	18,125	18,692	19,510	2,366	13.80
Capistrano Unified	18,308	18,306	18,435	18,896	20,137	1,829	9.99
Chino Unified	15,155	15,661	16,178	16,714	17,406	2,251	14.85
Compton Unified	30,003	28,783	28,333	27,870	28,522	(1,481)	-4.94
CONEJO VALLEY UNIFIED	19,712	19,179	18,681	18,311	18,539	(1,173)	-5.95
Corona-Norco Unified	16,430	16,422	16,383	16,618	17,006	576	3.51
East Side Union High	23,094	23,906	24,549	24,062	25,200	2,106	9.12
Elk Grove Unified	13,781	14,183	14,939	15,655	17,016	3,235	23.47
Fairfield-Suisun Valley Joint Unified	13,730	13,891	14,163	14,638	15,788	2,058	14.99
FONTANA UNIFIED	13,602	14,242	14,677	15,025	15,941	2,339	17.20
Fremont Unified	27,144	27,284	26,885	26,717	27,833	689	2.54
Garden Grove Unified	39,505	38,696	38,360	38,328	38,635	(870)	-2.20
Glendale Unified	19,854	19,996	19,967	19,654	20,044	190	0.96
Grossmont Union High	20,949	20,583	20,727	21,017	21,834	885	4.22
Hacienda-La Puente Unified	28,618	28,376	27,903	28,324	28,706	88	0.31
HAYWARD UNIFIED	19,915	19,855	19,671	19,897	20,245	330	1.66
Huntington Beach Union High	20,609	20,311	20,143	19,777	19,799	(810)	-3.93
Inglewood Unified	14,800	15,301	15,764	16,270	16,920	2,120	14.32
Irvine Unified	15,667	16,227	16,413	16,666	17,918	2,251	14.37
Kern Union High	16,393	16,304	16,884	17,872	19,714	3,321	20.26
Lodi Unified	15,589	16,094	16,815	17,750	18,729	3,140	20.14
Long Beach Unified	58,152	59,660	61,052	62,150	64,692	6,540	11.25
Los Angeles Unified	577,855	586,181	595,032	603,055	625,889	48,034	8.31
Montebello Unified	30,075	30,751	31,938	32,778	34,076	4,001	13.30
Mt. Diablo Unified	34,328	33,290	32,537	31,861	32,659	(1,669)	-4.86
NEWPORT-MESA UNIFIED	17,961	17,476	17,023	16,517	16,812	(1,149)	-6.40
Norwalk-La Mirada Unified	20,614	20,597	19,961	19,760	20,637	23	.11

*Central Unified School District was formed on July 1, 1982.

NOTE: District names in UPPER CASE were part of our sample of 25 LEAs that we determined face potential financial problems.

<u>Local Educational Agency</u>	<u>Fiscal Year 1981-82</u>	<u>Fiscal Year 1982-83</u>	<u>Fiscal Year 1983-84</u>	<u>Fiscal Year 1984-85</u>	<u>Fiscal Year 1985-86</u>	<u>Net Change</u>	<u>Percentage</u>
<u>Large School Districts (Continued)</u>							
Ontario-Montclair Elementary	15,546	15,988	15,992	15,853	16,540	994	6.39
Orange Unified	26,545	25,695	24,968	24,705	24,359	(2,186)	-8.24
Pasadena Unified	21,549	21,725	21,605	21,407	21,936	386	1.79
Placentia Unified	17,397	17,309	17,142	17,094	17,559	162	0.93
Pomona Unified	22,936	23,360	24,036	24,525	25,738	2,802	12.22
Poway Unified	15,206	15,318	15,387	15,895	17,224	2,018	13.27
RIVERSIDE UNIFIED	24,622	24,750	24,994	25,671	26,349	1,727	7.01
Rowland Unified	17,548	17,722	17,988	18,179	18,814	1,266	7.21
SACRAMENTO CITY UNIFIED	42,184	43,291	43,658	44,973	46,686	4,502	10.67
Saddleback Valley Unified	21,182	21,236	21,124	21,023	21,565	383	1.81
San Bernardino City Unified	28,702	29,122	29,810	30,713	32,903	4,201	14.64
San Diego Unified	109,155	108,554	108,952	109,317	112,491	3,336	3.06
SAN FRANCISCO UNIFIED	56,763	58,284	59,301	59,821	61,837	5,074	8.94
San Jose City Unified	34,341	33,457	32,073	31,941	32,193	(2,148)	-6.25
San Juan Unified	45,725	45,098	44,728	44,887	46,367	642	1.40
Santa Ana Unified	31,356	32,251	33,125	33,834	35,162	3,806	12.14
Simi Valley Unified	22,071	21,424	20,922	20,392	20,619	(1,452)	-6.58
Torrance Unified	24,231	23,833	23,064	23,002	23,217	(1,014)	-4.18
Visalia Unified	15,948	16,452	17,075	17,609	18,443	2,495	15.64
Subtotals	<u>1,803,167</u>	<u>1,814,869</u>	<u>1,827,635</u>	<u>1,844,684</u>	<u>1,906,832</u>	<u>103,665</u>	<u>5.75</u>
Grand Totals	<u>2,181,764</u>	<u>2,185,916</u>	<u>2,182,191</u>	<u>2,188,581</u>	<u>2,253,889</u>	<u>72,125</u>	<u>3.31</u>

NOTE: District names in UPPER CASE were part of our sample of 25 LEAs that we determined face potential financial problems.

APPENDIX D

ASSUMPTIONS WE USED IN PREPARING FUND BALANCE PROJECTIONS FOR THE EIGHT LOCAL EDUCATIONAL AGENCIES WE VISITED

In preparing the fund balance projections for June 30, 1987, we made the following material assumptions and adjustments:

1. The forecasted revenues are based on the most complete data available from the State Department of Education, the Board of Governors of the California Community Colleges, the individual local educational agencies, and the county offices of education. The information obtained includes base revenue limit worksheets, data on average daily attendance, lottery estimates, county tax income estimates, federal and state notifications of grants, contracts, and other supporting documentation. In addition, some of the State's programs were not fully funded when we prepared the forecasts. In prior years, the Legislature has generally provided the additional revenues through special legislation. However, because we cannot predict whether the Legislature will pass a similar funding bill in the current fiscal year, we have not included these revenues in our forecast.
2. The forecasted revenues do not include a \$3.3 million emergency apportionment Peralta Community College District may receive during the current fiscal year. Peralta Community College District will be required to repay the amount received, including interest, in the next three fiscal years.
3. The forecasted expenditures and contingencies are based on the pattern of actual expenditures to date, historical expenditure trends, current contractual agreements, and other events and circumstances that effect current year expenditures.
4. The beginning fund balance is based on the fiscal year 1985-86 audited financial statements, which include prior period adjustments, the write-off of uncollectible balance sheet items, and the elimination of funds not representative of the General Fund.
5. The forecasted reserves are based on assumptions concerning future events and circumstances. Because some assumptions may not materialize and unanticipated events and circumstances may occur after the date of this forecast, the actual results during the forecast period may differ from the forecasted results. These differences may be material.



CALIFORNIA STATE DEPARTMENT OF EDUCATION

Bill Honig**721 Capitol Mall; P.O. Box 944272****Superintendent****Sacramento, CA 94244-2720**

of Public Instruction

March 18, 1987

Thomas W. Hayes, Auditor General
Office of the Auditor General
660 J Street Suite 300
Sacramento, CA 95814

RE: F-637

Dear Mr. Hayes:

Thank you for the opportunity to review the draft report titled "A Review of the Financial Condition of School Districts, County Offices of Education, and Community College Districts in California." This study documents many of the fiscal management problems we have known were facing local educational agencies.

We generally concur with the findings regarding the seemingly high number of districts with low reserves. The continuing and competing demands on all available funds, and in some cases reserve balances as well, have become more intense in recent years. As a result, we agree that there are an unusually large number of local educational agencies that will be solvent next year only if they make significant budget reductions, particularly in view of the Governor's 1987-88 budget proposal.

It is important for the reader to note that a number of the findings in this report are drawn from a sample of eight districts which were purposefully selected as having fiscal problems. (*) Care should be taken in drawing inferences regarding the overall universe of districts. Of the 1,086 K-12 local educational agencies, only six received loans in the past five years.

School district budgeting is a difficult job that is made even more so by factors outside the control of local school districts. Particular examples noted in the report include the differential cost of living adjustments (COLAs) provided by the annual Budget Act and the growing number of categorical programs which require expenditures in excess of the appropriations provided. Both differential COLAs and categorical programs which are not self-supporting represent a growing encroachment problem for the relatively modest unrestricted general fund revenues of most school districts. For all practical purposes employees with similar responsibilities must be given the same salary adjustment under collective bargaining even if the Budget Act does not provide for comparable inflationary adjustments across all categorical programs.

Auditor General's Comment:

- * We visited only 8 LEAs; however, we analyzed the financial data of an additional 124 LEAs. Many of these exhibited the same financial problems as the districts we visited, specifically, low reserves and deficit spending.

Thomas W. Hayes
March 18, 1987
Page 2

Similarly, categorical programs like special education by law must be provided even when state entitlements are not designed to cover all of the costs of program operation. In the face of increasing pressure to improve programs and implement reforms, the general fund encroachment caused by these state level policy decisions makes it increasingly difficult to maintain adequate reserves and balanced budgets.

The special education funding problem noted in the report has been a concern for at least six years. The Special Education Task Force established in this year's Budget Act is the most recent effort in seeking to solve this major funding issue. The Task Force is to analyze special education cost data, and to develop recommended changes to the program's existing funding model. In addition to changing the base year used to compute funding levels, the Task Force's goal is to develop a consistent funding model that is characterized by service equity, minimal need for waivers, and which remains internally responsive to changing needs throughout the State. An interim report was submitted earlier this month to the Joint Legislative Budget Committee and the Department of Finance. A final report, including recommendations for legislation, will be submitted by November 15, 1987.

In response to the recommendations concerning the administrator-teacher ratio calculation, the Department proposes to implement several changes in the data collection in 1987-88. Changes in the California Basic Educational Data System (CBEDS) Manual of Instructions are as follows: 1) provide more detailed definitions of the teacher, administrator, exempted administrator and pupil services employee classifications; 2) clarify language relating to employees with assignments in the adult education program; and 3) clarify instructions to ensure the omission of child development teachers. Additionally, the CBEDS County/District Information Form will be modified to collect full time equivalents of certificated staff in the adult education program and the adult education staff will be included in the initial computation of administrator-teacher ratios in 1987-88.

We view the findings regarding the early warning system and the recommendations for legislative changes as somewhat premature. The system is new, having been established in 1985 and modified by legislation effective January 1, 1987. We would prefer to take more time to assess the system, at least until the end of this fiscal year, before making changes. We recommend that after the close of the 1986/87 fiscal year, the K-12 early warning system be examined by the Superintendent's Fiscal Management

Thomas W. Hayes
March 18, 1987
Page 3

Advisory Committee and that the committee report to the Legislature no later than October 1, 1987. The report would review the early warning system and propose any changes the committee believes to be necessary, giving particular attention to the issues raised in your report. Representatives of your office, the State Controller's Office, the Department of Finance, the Legislature, labor and professional organizations and local educational agencies serve on this committee.

We appreciate the efforts of your staff in preparing such a comprehensive report in a relatively short timeframe.

Sincerely,

A handwritten signature in dark ink, appearing to read "William D. Dawson". The signature is fluid and cursive, with a large initial "W" and "D".

William D. Dawson
Executive Deputy Superintendent

WDD:c

BOARD OF GOVERNORS OF THE
CALIFORNIA COMMUNITY COLLEGES
RESPONSE TO THE AUDITOR GENERAL'S REPORT

The Board of Governors of the California Community Colleges chose not to provide written comments; however, we discussed the draft report with the board of governors.

**cc: Members of the Legislature
Office of the Governor
Office of the Lieutenant Governor
State Controller
Legislative Analyst
Assembly Office of Research
Senate Office of Research
Assembly Majority/Minority Consultants
Senate Majority/Minority Consultants
Capitol Press Corps**